1995

Compilation and Review Manual, Volume 2

O. Ray Whittington

Alan J. Winters

Anita M. Lyons

AICPA

Compilation and Review Manual

INTEGRATED PRACTICE SYSTEM

VOLUME 2

AICPA

VOLUME 2

Compilation and Review Manual

AICPA

INTEGRATED

PRACTICE

SYSTEM

AICPA

VOLUME 2

Compilation and Review Manual

Authors:
O. Ray Whittington, CPA
Alan J. Winters, CPA

AICPA
INTEGRATED
PRACTICE
SYSTEM

AICPA

VOLUME 2

Compilation and Review Manual

Authors:
O. Ray Whittington, CPA
Alan J. Winters, CPA

Editor:
Anita M. Lyons, CPA

AICPA

INTEGRATED

PRACTICE

SYSTEM

This manual has not been approved, disapproved, or otherwise acted upon by any senior technical committees of the American Institute of Certified Public Accountants or the Financial Accounting Standards Board and has no official or authoritative status.

The manual is issued as a nonauthoritative kit of practice aids and is not intended as a substitute for professional judgments or for authoritative technical literature.

The documentation in this manual is not a substitute for development and implementation by a firm of a system of quality control that is appropriately comprehensive and suitably designed in relation to the firm's organizational structure, its policies, and the nature of its practice.

1 2 3 4 5 6 7 8 9 0 TI 9 9 8 7 6 5

TABLE OF CONTENTS

VOLUME 1

VOLUME 2

Comparative
Financial Statements

CHAPTER 8

REPORTING ON COMPARATIVE FINANCIAL STATEMENTS

Table of Contents

CHAPTER 8

REPORTING ON COMPARATIVE FINANCIAL STATEMENTS

Table of Contents (Continued)

Table of Contents (Continued)

Table of Contents (Continued)

CHAPTER 8

REPORTING ON COMPARATIVE FINANCIAL STATEMENTS

8.000 INTRODUCTION

8.001 Often the financial statements of two or more periods will be presented in columnar form. Such financial statements are defined as comparative financial statements and Statement on Standards for Accounting and Review Services (SSARS) No. 2 requires that each period must be reported on. This chapter provides guidance about —

- Who should report on those statements when the prior-period financial statements have been audited, reviewed, or compiled by another accountant.
- What the accountant's report(s) should say.
- What procedures, if any, the accountant(s) should perform.

Practice Tip:

If prior-period financial statements are not presented in columnar form, they do not meet the SSARS No. 2 definition of comparative financial statements, and are not subject to the reporting requirements of SSARS No. 2. In addition, the requirements of SSARS No. 2 do not apply to prior-period financial statements in a client-prepared document that are presented on separate pages from the financial statements that are reported on by the accountant. However, the document should include an indication (generally, on the face of the financial statements) that the accountant has not compiled or reviewed the prior-period financial statements and assumes no responsibility for them.

8.002 Reporting on comparative financial statements can range from simple, straight-forward situations to complex situations affected by several different conditions. In general, accountants reporting on comparative financial statements must consider whether one or more of the following conditions exist and, if so, how they affect both the engagement's reporting and performance requirements:

- The accountant reporting on the current-period financial statements did not previously report on all prior-period financial statements presented (section 8.200).

- The accountant reporting on the current-period financial statements previously reported on all prior-period financial statements presented (section 8.300).
- The levels of service provided for each period are different (section 8.300).
- Additional information has become available about previously issued comparative financial statements that might affect the previous report(s) (sections 8.200, 8.300, and 8.400).
- The status of the reporting entity has changed from nonpublic to public or vice versa (section 8.500).

The effects of these conditions on both the accountant's reporting and performance requirements are discussed in detail in this chapter. Section 8.600 of this Chapter includes illustrative reports appropriate for these conditions.

8.100 WHO SHOULD REPORT ON COMPARATIVE STATEMENTS?

8.101 If different accountants compiled or reviewed the two-or-more period financial statements presented, a question arises as to who should report on the comparative financial statements. The first two conditions listed in section 8.002 address this question. The answer to the question determines both the reporting and performance requirements for the comparative financial statements.

8.102 When the accountant who is reporting on the current period previously reported on all prior periods presented, that accountant is considered to be a *continuing accountant* as defined in SSARS No. 2. A continuing accountant is required to issue a report or reports in the current period that cover all periods presented for comparative purposes.

8.103 When the accountant reporting on the current-period financial statements did not previously report on all prior periods presented, the accountant must determine if he or she meets the definition of a continuing accountant contained in SSARS No. 2. A continuing accountant is one who has been engaged to compile, review, or audit the current-period financial statements and one or more consecutive periods immediately prior to the current period.

8.104 The key to determining whether the current accountant is a continuing accountant lies in the terms *consecutive* and *immediately prior*. If the current accountant has reported on one or more consecutive periods immediately preceding the current period, he or she is considered to be a continuing accountant with respect to those periods. For example, assume a client presents comparative financial statements for the current year, 19X3, and for the preceding year, 19X2. If CPA firm X reported on the 19X2 financial statements and is engaged to report on the 19X3 financial statements, then CPA firm X is considered a continuing accountant for purposes of reporting on those periods. If CPA firm Y reported on the 19X2 financial statements, then CPA firm X is not a continuing accountant.

8.105 SSARS No. 2 bases its discussion and report illustrations on comparative statements presented for two periods. However, comparative statements may be presented for more than two periods and such presentations may create more complex reporting considerations. For example, assume a client presents comparative financial statements for the current year, 19X3, and for the two preceding years, 19X2 and 19X1. If CPA firm X reported on both 19X2 and 19X1 and is engaged to report on 19X3, then CPA firm

X is a continuing accountant for purposes of reporting on all three years. However, if CPA firm X reported on 19X2 and is engaged to report on 19X3 but CPA firm Y reported on 19X1, then CPA firm X is a continuing accountant for purposes of reporting on the 19X3 and 19X2 financial statements and is considered a successor accountant for purposes of reporting on the 19X1 financial statements.

8.106 In summary, when only two periods are presented for comparative purposes, the current accountant is either a continuing accountant or a successor accountant. However, when more than two periods are presented, the current accountant may fall into one of three categories--(a) a continuing accountant only, (b) a successor accountant only, or (c) both a continuing and successor accountant. Determining in which category the current accountant falls is important because the performance and reporting responsibilities differ for each category. Illustration 8-1 presents a decision chart to assist in determining which category the accountant is in.

8.107 If the accountant is exclusively a continuing accountant, he or she needs to consider the guidance in section 8.300 only. The guidance in section 8.200 *will not* apply to the engagement.

8.108 If the accountant is exclusively a successor accountant, he or she needs to consider the guidance in section 8.200 only. The guidance in section 8.300 *will not* apply to the engagement.

8.109 If the accountant is both a continuing accountant and a successor accountant, he or she needs to consider the guidance in both section 8.200 and section 8.300. The guidance in section 8.300 applies to the accountant's responsibility for the period(s) on which he or she reported and the guidance in section 8.200 defines the accountant's responsibility for the period(s) on which another accountant reported.

Illustration 8-1

Determining the Status of the Accountant for Reporting on Comparative Financial Statements

Engagement Terms	Type of Accountant
1. You are engaged to report on the current period and you previously reported on all prior-period financial statements presented for comparative purposes.	CONTINUING ACCOUNTANT ONLY
2. You are engaged to report on the current period but another accountant previously reported on all prior-period financial statements presented for comparative purposes.	SUCCESSOR ACCOUNTANT ONLY
3. You are engaged to report on the current period and you previously reported on at least the immediately preceding period but another accountant previously reported on other prior-period financial statements presented for comparative purposes.	CONTINUING ACCOUNTANT FOR PURPOSES OF PRIOR PERIODS YOU REPORTED ON AND SUCCESSOR ACCOUNTANT FOR PURPOSES OF THE PERIODS REPORTED ON BY THE OTHER ACCOUNTANT

4. You are not engaged to report on the current period but you reported on at least one of the prior-period financial statements presented for comparative purposes.	PREDECESSOR ACCOUNTANT ONLY

8.200 REPORTING AS A SUCCESSOR ACCOUNTANT

8.201 When another accountant previously reported on one or more of the prior periods presented, paragraph 16 of SSARS No. 2 allows the accountant who is reporting on the current period (the successor accountant) one of the following three alternatives:

- Have the client request the other accountant (the predecessor accountant) to reissue his or her report on the prior period(s).
- Make reference to the predecessor accountant's report in his or her current-period report.
- Perform a compilation, review, or audit of the financial statements of the prior period(s) and issue his or her own report on that period(s).

Predecessor Reissues Report

8.202 The client may request the predecessor accountant to reissue his or her compilation or review report on prior-period financial statements. The predecessor accountant, however, is not required to reissue a report and may decline the client's request.

8.203 If the predecessor agrees to reissue the report, he or she must decide whether the previously issued report is still appropriate. In making that decision, paragraph 20 of SSARS No. 2 requires the predecessor accountant to consider the following factors:

- The current form and manner of presentation of the prior-period financial statements (i.e., Have they in any way been changed from the original presentation?).
- Subsequent events not previously known.
- Changes in the financial statements that require the addition or deletion of modifications to the standard report (i.e., Should the original report be changed because of changes in the prior-period financial statements?).

8.204 To appropriately consider the factors in section 8.203, paragraph 21 of SSARS No. 2 requires the predecessor accountant to perform the following procedures before reissuing a report:

a. Read the financial statements of the current period and the successor accountant's report on them.

b. Compare the prior-period financial statements (as they will appear in the comparative presentation) with those previously issued and with those of the current period.

c. Obtain a letter from the successor accountant that indicates whether he or she is aware of any matter that, in his or her opinion, might have a material effect on the financial statements, including disclosures, reported on by the predecessor accountant. The predecessor accountant should not refer in his or her reissued report to this letter or to the successor accountant's report.

8.205 The results of the procedures in section 8.204, along with other sources, may make the predecessor accountant aware of information that may affect the prior-period financial statements or his or her report on them. When such information is obtained, the predecessor accountant is required by paragraph 22 of SSARS No. 2 to—

a. Make inquiries or perform analytical procedures similar to those he or she would have performed if he or she had been aware of the information at the date of the report on the prior-period financial statements

b. Perform any other procedures he or she considers necessary in the circumstances, such as discussing the information with the successor or reviewing the successor accountant's working papers

8.206 No Changes in Prior Statements or Report. If the predecessor accountant decides based on the above procedures that the prior-period financial statements should not be restated and his or her report on them should not be revised, then the predecessor accountant may reissue his or her previous report. The reissued report should be dated as of the date of the previous report to avoid the implication that any procedures other than those in sections 8.203 through 8.205 have been performed.

8.207 Changes in Prior Statements or Report. If the predecessor accountant decides based on the above procedures that the prior-period financial statements should be restated or his or her report on them should be revised, the reissued report should be modified in two ways: (1) a separate explanatory paragraph should be added, and (2) the report should be dual dated. (See sections 8.402 through 8.405 for a discussion and illustration of this report modification.)

8.208 When the prior-period financial statements are restated or the predecessor accountant revises his or her report on them, paragraph 23 of SSARS No. 2 requires the predecessor accountant to obtain a written statement from the former client. That statement should describe the reasons for restating the prior-period financial statements and, if applicable, express an understanding of its effect on the predecessor accountant's reissued report.

8.209 If the predecessor accountant is unable to complete the procedures required by SSARS No. 2 (described in sections 8.203 through 8.205 and 8.208), he or she should not reissue his or her report and may wish to consult with his or her attorney regarding the appropriate course of action.

Successor Accountant Refers to Predecessor Accountant's Report

8.210 In most circumstances, the predecessor accountant will not be asked to reissue his or her report on prior-period financial statements, or he or she will refuse such a request (and the successor accountant will not have compiled or reviewed those financial statements). The successor accountant, therefore, will usually decide to refer in his or her report on the comparative financial statements to the predecessor accountant's report. This reference should be made in an additional paragraph of the successor's report and should contain the following information:

a. A statement that the prior-period financial statements were compiled or reviewed by another accountant (or accountants)

b. The date of such report

c. A description of the standard form of disclaimer (compilation) or limited assurance (review), as applicable, included in the predecessor accountant's report

d. A description or quotation of any modification of the standard report and of any paragraphs emphasizing a matter regarding the financial statements

Although paragraph 17 of SSARS No. 2 requires the successor accountant's report to state that a predecessor accountant compiled or reviewed the prior-period financial statements, footnote 9 to that paragraph prohibits the successor accountant from naming the predecessor accountant in his or her report. (See sections 8.603 through 8.606 for illustrative successor accountant's reports that refer to the predecessor accountant's report.)

8.211 In some situations, the successor accountant may believe that prior-period financial statements reported on by a predecessor accountant should be restated. In that event, the successor accountant cannot refer to the predecessor accountant's report on those financial statements but should instead choose one of the following two options:

a. Request that the predecessor accountant reissue his or her report based on the guidance in sections 8.202 through 8.209 and sections 8.402 through 8.405.

b. Compile or review those financial statements in accordance with SSARS No. 1, or audit them in accordance with generally accepted auditing standards (See sections 8.212 and 8.213.)

The successor accountant should also remember that in such a situation, SSARS No. 4, paragraph 10, requires the successor accountant to request that the client notify the predecessor accountant that the prior-period financial statements need to be restated. If the client refuses to do so, or the successor accountant is not satisfied with the predecessor accountant's course of action, the successor accountant should consult with his or her attorney.

Practice Tip:

When the successor accountant becomes aware of information that leads him or her to believe that financial statements reported on by a predecessor *who has ceased operations* may require revision, the successor's responsibility is not changed. Instead of advising the predecessor, the client should advise the party responsible for winding up the affairs of the predecessor firm.

Successor Accountant Compiles, Reviews, or Audits Prior-Period Financial Statements

8.212 The successor accountant may decide to compile or review the prior-period financial statements presented for comparative purposes. When compiling or reviewing the prior-period financial statements, the accountant should follow the *performance* requirements for compiling or reviewing those financial statements in SSARS No. 1. (See Chapter 4 or 6 in this Manual.) In addition, the successor accountant should follow the *reporting* guidance provided below in section 8.300 for a continuing accountant.

8.213 If the successor accountant decides to audit the prior-period financial statements, he or she should follow the performance and reporting guidance in generally accepted auditing standards. Note that the AICPA Auditing Standards Board issued an interpretation of SAS No. 7, *Communications Between Predecessor and Successor Auditors* (Au 315), titled *Audits of Financial Statements That Had Been Previously Audited By A Predecessor Auditor* (Au 9315.08-.18) in 1995.

Which Choice Is Preferable?

8.214 In summary, the successor accountant has three alternatives for reporting on prior-period financial statements that are compiled, reviewed, or audited by another accountant. As a general rule, the second alternative (make reference to the predecessor accountant's report) requires the least effort and expense, because the predecessor accountant does not need to become involved. However, as discussed below, certain circumstances may make another alternative preferable.

8.215 The first alternative (have the predecessor accountant reissue his or her report) may be preferable in cases where the prior-period financial statements are restated, for example, for correction of an error. The additional work required by the predecessor accountant to reissue his or her report on the restated prior-period financial statements may be less than the work required by the successor accountant to compile or review those financial statements. This is often the case when the client needs a review report covering both the current and prior-period financial statements.

8.216 The third alternative (compile, review, or audit the prior-period financial statements) is a back-up alternative that can be selected whenever it makes sense.

Reporting by a Successor Accountant When Predecessor Has Ceased Operations

8.217 If prior-period financial statements that have been compiled, reviewed, or audited by a predecessor accountant who has ceased operations are presented for comparative purposes with current-period compiled or reviewed financial statements, the successor's reporting responsibility is set forth below for the following three circumstances:

1. The prior-period financial statements were compiled or reviewed and are unchanged. (Sections 8.218–.219)

2. The prior-period financial statements were audited and are unchanged. (Sections 8.220–.221)

3. The prior-period financial statements have been restated. (Section 8.222)

8.218 If the prior-period financial statements were compiled or reviewed and are unchanged, the successor should add a paragraph to his or her report on the current-period financial statements that includes —

a. A statement that the financial statements of the prior period were compiled or reviewed by another accountant who has ceased operations,

b. The date of the predecessor's report,

c. A description of the standard form of disclaimer or limited assurance, as applicable, and

d. A description or a quotation of any modifications of the standard report and of any paragraphs emphasizing a matter concerning the financial statements.

8.219 Reference to the predecessor's report should not include the predecessor's name. Examples of additional paragraphs are presented below.

Compiled Prior-Period Financial Statements

The 19X1 financial statements of XYZ Company were compiled by other accountants who have ceased operations and whose report dated February 1, 19X2 stated that they did not express an opinion or any other form of assurance on those statements.

Reviewed Prior-Period Financial Statements

The 19X1 financial statements of XYZ Company were reviewed by other accountants who have ceased operations and whose report dated March 1, 19X2 stated that they were not aware of any material modifications that should be made to those statements in order for them to be in conformity with generally accepted accounting principles.

8.220 If the prior-period financial statements were audited and are unchanged, the successor should add a paragraph to his or her report on the current-period financial statements that indicates —

a. The prior-period financial statements were audited by another accountant who has ceased operations,

b. The date of the predecessor's report,

c. The type of opinion issued by the predecessor,

d. If the opinion was other than qualified, the substantive reasons therefor, and

e. That no auditing procedures were performed after the date of the predecessor's report.

8.221 Reference to the predecessor's report should not include the predecessor's name. An example of such paragraph is presented below.

> The financial statements for the year ended December 31, 19X1, were audited by other accountants who have ceased operations, and they expressed an unqualified opinion on them in their report dated March 1, 19X2, but they have not performed any auditing procedures since that date.

8.222 If the prior-period financial statements have been restated, the restated prior-period financial statements should be compiled, reviewed, or audited and reported on accordingly.

8.300 REPORTING AS A CONTINUING ACCOUNTANT

8.301 When the accountant who is reporting on the current-period financial statements meets the definition of a continuing accountant, he or she must issue a report in the current period that covers all comparative financial statements on which he or she previously reported. The accountant's responsibility for such reporting is determined by considering the following two questions:

- Is the level of service for the current period the same as, higher than, or lower than the level of service for the prior period?
- Has additional information become available about previously issued comparative financial statements that might affect the previous report(s)?

Level of Service — General

8.302 Four levels of service may be provided on the financial statements of a nonpublic entity. These are: (1) audit, (2) review, (3) compilation with full disclosures, and (4) compilation with substantially all disclosures omitted. To determine his or her reporting responsibility, a continuing accountant must compare the level of service provided for the current period with the level of service provided in the prior period. (Changes involving the fourth level of service, compilation of financial statements that omit substantially all disclosures, are discussed separately from other changes. See sections 8.312 through 8.315.)

Same or Higher Level of Service in Current Period

8.303 If the level of service for the current period is the same as or higher than that for the prior period, the accountant is required to *update* his or her report on the prior-period financial statements. Updating a prior-period report means that the accountant is issuing a report on the prior-period financial statements as of the date of the report on the current-period financial statements. When the accountant updates his or her report, the accountant is obligated to consider information he or she becomes aware of during the current engagement. Based on this information, the accountant may re-express his or her previous conclusions or may express different conclusions on the prior-period financial statements. (See sections 8.406 through 8.412 for a discussion of reports that express different conclusions about prior-period financial statements.)

8.304 Compilation in Current and Prior Period. When the financial statements of both periods have been compiled, the accountant simply drafts the first paragraph of the report to refer to the financial statements of both periods. An illustration of this paragraph follows:

> I (We) have compiled the accompanying balance sheets of ANY Company as of December 31, 19X2 and 19X1, and the related statements of income, retained earnings, and cash flows for the years then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

(See section 8.607 for an illustration of a complete report.)

8.305 Review in Current and Prior Period. When the financial statements of both periods have been reviewed, the accountant drafts the first paragraph of the report to refer to the financial statements of both periods and drafts the third paragraph to refer to both reviews. These paragraphs are illustrated below:

(First Paragraph)

> I (We) have reviewed the accompanying balance sheets of ANY Company as of December 31, 19X2 and 19X1, and the related statements of income, retained earnings, and cash flows for the years then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of the company.

(Third Paragraph)

> Based on my (our) reviews, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

(See section 8.608 for an illustration of a complete report.)

8.306 Current Period Reviewed — Prior Period Compiled. When the current-period financial statements have been reviewed and the prior-period financial statements were compiled (change from a lower to a higher level of service), the first paragraph of the report *cannot* be written to refer to the financial statements of both periods. The language of the first paragraph of the standard review report differs from that of the standard compilation report. Therefore, the report modification is made by adding a fourth paragraph to the standard review report on the current-period financial statements. This paragraph updates the compilation report on the prior-period financial statements. An illustration of this paragraph follows:

> The accompanying 19X1 financial statements of ANY Company were compiled by me (us) in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the 19X1 financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

(See section 8.609 for an illustration of a complete report.)

8.307 Current Period Audited — Prior Period Reviewed or Compiled. SSARS do not apply to presentations of comparative financial statements when the current period is audited and prior periods are either compiled or reviewed. Statements on Auditing Standards (SASs) apply to such presentations and the accountant should refer to SAS No. 26, *Association with Financial Statements,* for guidance on these presentations.

Lower Level of Service in Current Period

8.308 If the level of service in the current period is lower than that of the prior period, the accountant is not required to update his or her report. Instead, the accountant either (1) reissues his or her report on the prior-period financial statements or, (2) includes a separate paragraph in the current period report that describes the responsibility assumed for the prior-period financial statements.

8.309 A *reissued* report is essentially a duplicate of the original report. A reissued report bears the same date as the original report and usually repeats the conclusions presented in the original report. However, a reissued report may need to be revised if the accountant has become aware of specific events that might affect the prior-period financial statements. (When a previously issued report is revised, see sections 8.410 through 8.412.)

8.310 If the accountant elects to reissue his or her report on the prior-period financial statements, that report may be presented separately from the current-period report or may be combined with it. When the accountant combines the prior-period report with the current-period report, the combined report should state that the accountant has not performed any procedures in connection with the previous engagement after the date of the previous report. (See section 8.610 for a report that illustrates a reissued review report combined with a current-period compilation report.)

8.311 If the accountant elects to include a separate paragraph in the current-period report that describes his or her responsibility for the prior-period financial statements, that paragraph should state —

- The date of the prior-period financial statements.
- The service provided in the prior period.
- The date of the accountant's previous report.
- The conclusions in the previous report.
- That the accountant has not performed any procedures in connection with the prior engagement subsequent to the date of his or her report on that engagement.

(See sections 8.611, 8.612, and 8.613 for illustrative reports.)

Changes in Level of Service — Substantially All Disclosures Omitted

8.312 Although an accountant may compile financial statements that omit substantially *all* disclosures (OSAD statements), paragraph 5 of SSARS No. 2 states that such financial statements are not comparable to financial statements that include disclosures. Therefore, an accountant can report on comparative financial statements that omit substantially all disclosures only when all comparative financial statements omit disclosures. Reporting on comparative periods that mix full disclosure statements and OSAD statements is prohibited.

8.313 When the accountant is engaged to report on current-period financial statements that omit substantially all disclosures and has also previously reported on the compilation of similar financial statements for the prior period, the first paragraph of the standard OSAD compilation report is drafted to refer to the financial statements of both periods. An illustration of this paragraph is presented below:

> I (We) have compiled the accompanying balance sheets of ANY Company as of December 31, 19X2 and 19X1, and the related statements of income, retained earnings, and cash flows for the years then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

(See section 8.614 for an illustration of a complete report.)

8.314 In some engagements, the accountant may be engaged to provide an OSAD compilation report on current-period financial statements when the prior-period financial statements were full disclosure statements that were either audited, reviewed, or compiled. In these situations, SSARS No. 2 permits the accountant to compile OSAD statements for the prior period so that comparative statements may be presented. That is, full disclosure statements for the prior period may effectively be *converted* to OSAD statements. This conversion is accomplished by eliminating the disclosures and indicating in the accountant's current-period report the nature of the previous service rendered (audit, review, or compilation) and the date of the previous report. (See section 8.615 for an illustrative report.)

8.315 If the previous financial statements were audited and the opinion on those statements was other than unqualified, the accountant's current-period report should also indicate the type of opinion expressed (qualified, adverse, or disclaimer) and the substantive reasons for the modified opinion. Similarly, if the prior-period financial statements were reviewed or compiled and the accountant issued a modified review or compilation report, or added an emphasis-of-a-matter paragraph to the report, the accountant's current-period report should also contain a description or quotation of the modification or emphasis paragraph.

8.400 REVISIONS OF PRIOR-PERIOD FINANCIAL STATEMENTS OR THE ACCOUNTANT'S REPORT

8.401 Several circumstances may require revision of prior-period financial statements, including the following:

- Change from an accounting principle that is not generally accepted to one that is for prior-period financial statements.
- Change from one generally accepted accounting principle to another generally accepted accounting principle that requires retroactive restatement of prior-period financial statements.
- Correction of clerical or mathematical errors in the prior-period financial statements.
- Subsequent events have occurred since the issuance of the accountant's original report that require adjustment of or disclosure in the prior-period financial statements.

When the financial statements of a prior period have been changed, either the predecessor or the current accountant should report on them as restated. (See sections 8.616, 8.617, and 8.618 for illustrative reports.)

Predecessor Accountant Reports on Restated Financial Statements

8.402 As discussed in section 8.207, a predecessor accountant who has been engaged to reissue his or her report on prior-period financial statements may conclude that those financial statements should be restated. In such circumstances, the predecessor accountant's reissued report should (1) include a separate explanatory paragraph, and (2) be dual-dated.

8.403 The separate explanatory paragraph should indicate —

a. The date of the accountant's previous report

b. The circumstances or events that caused either a new reference to a departure from generally accepted accounting principles (GAAP) (or other comprehensive bases of accounting [OCBOA]) or a removal of a reference to a departure from GAAP (OCBOA) in the previous report

c. That the financial statements of the prior period have been changed

8.404 An example of such a separate explanatory paragraph is presented below:

> In my (our) previous compilation (review) report dated March 1, 19X2, on the 19X1 financial statements, I (we) referred to a departure from generally accepted accounting principles because the company carried its land at appraised values. However, as disclosed in Note X, the company has restated its 19X1 financial statements to reflect its land at cost in accordance with generally accepted accounting principles.

8.405 Dual-dating means that two dates are included in the report. One date is the date of the previous report and the other date is the date of the event or transaction that caused the financial statements to be restated or the report to be revised. For example, a dual-dated report would read as follows "March 1, 19X1, except for Note X, as to which the date is March 15, 19X2." In this example, March 1, 19X1 is the date of the previous report and March 15, 19X2 is the date the subsequent event described in Note X occurred. Dual-dating limits the predecessor's responsibility for events occurring subsequent to the completion of his or her engagement to the specific event referred to in the note (or disclosed in the report). (See section 8.618 for an illustrative report).

Current Accountant Reports on Restated Statements

8.406 When the accountant engaged to report on the current-period financial statements also reports on restated prior-period financial statements, the specific reporting requirements depend on whether the current accountant is a successor accountant or a continuing accountant with respect to the prior period.

8.407 Current Accountant Is Successor Accountant. If the current accountant is a successor accountant, then he or she has not previously reported on the prior-period financial statements and does not have a report to reissue or update. Therefore, he or she should perform a compilation or review of the prior-period financial statements in accordance with SSARS No. 1 or an audit of those statements in accordance with generally accepted auditing standards.

8.408 The successor's report on the restated prior-period financial statements may be issued separately from his or her report on the current period or combined with his or her report on the current-period financial statements. Regardless of the method of reporting, the successor accountant's report on the restated financial statements should not refer to the predecessor accountant's previously issued report.

8.409 If the restatement does not involve a change in accounting principles or their application (for example, it involves the correction of an error), paragraph 26 of SSARS No. 2 states that the accountant may wish to add an explanatory paragraph with respect to the restatement, but should not otherwise modify the standard report provided the financial statements appropriately disclose such matters. This guidance applies when either the successor or predecessor accountant reports on the restated prior-period financial statements.

8.410 Current Accountant Is Continuing Accountant. If the current accountant is a continuing accountant, then the accountant must either update or reissue his or her previously issued report on the restated prior-period financial statements. As discussed in sections 8.303 through 8.307, when the level of service for the current period is the same as or higher than the level of service for the prior period, the accountant must update his or her report. An updated report on restated prior-period financial statements should be dated as of the same date as the current-period report.

8.411 When the level of service for the current period is lower than the level of service for the prior period, the accountant should reissue his or her report using the original date of that report, as discussed in sections 8.308 through 8.311.

8.412 Regardless of whether an updated or reissued report is appropriate (e.g., regardless of the direction of change in the level of service) the report should contain the separate explanatory paragraph discussed and illustrated in sections 8.403 and 8.404.

8.500 CHANGE OF ENTITY STATUS

8.501 An entity may change its status from a public to a nonpublic entity or from a nonpublic to a public entity. SSARS No. 2, paragraph 31, states that the current status of the entity should determine whether the accountant should follow SSARS or generally accepted auditing standards. The current status of the entity should be determined as of its current balance-sheet date.

8.502 The basic principle for reporting on comparative financial statements when the entity has changed its status is that a previously issued report that is no longer appropriate for the current status of the entity should not be reissued or referred to in the current-period report. The remainder of this section discusses the application of this principle.

Change from Public to Nonpublic Entity

8.503 When the entity's current status is nonpublic but it was public for a prior period, SSARS must be followed in reporting on all periods presented. In this situation, the prior-period financial statements will have either a previously-issued unaudited disclaimer in accordance with SAS No. 26, or a previously-issued audit report.

8.504 If the report on the prior-period financial statements was an unaudited disclaimer, the accountant should either compile or review those statements in accordance with SSARS No. 1 and report on them accordingly. This is necessary because a SAS No. 26 disclaimer of opinion is inappropriate for a nonpublic entity.

8.505 If the report on the prior-period financial statements was an audit report, the accountant should either (1) reissue the prior-period audit report, or (2) include a separate paragraph in the current-period report. These reporting alternatives are acceptable because an audit report is appropriate for a nonpublic as well as a public company. When the accountant elects to include a separate paragraph, that paragraph should indicate—

a. That the financial statements of the prior period were audited previously

b. The date of the previous report

c. The type of opinion expressed previously

d. The substantive reasons for other than an unqualified opinion

e. That no auditing procedures were performed after the date of the previous report

An example of such a paragraph follows:

> The financial statements for the year ended December 31, 19X1, were audited by us (other accountants) and we (they) expressed an unqualified opinion on them in our (their) report dated March 1, 19X2, but we (they) have not performed any auditing procedures since that date.

Change from Nonpublic to Public Entity

8.506 When the entity's current status is public but was nonpublic for a prior period, SSARS do not apply. The accountant must follow generally accepted auditing standards in reporting for all periods presented.

Sample Reports —
Comparative Statements

8.600 SAMPLE REPORTS ON COMPARATIVE STATEMENTS

8.601 The following pages are illustrative reports for various situations involving the presentation of comparative financial statements.

8.602 The illustrative reports are included on the Wordperfect diskette provided with the manual.

Sample Reports on Comparative Statements

Sample Reports on Comparative Statements (Continued)

8.603 Successor Accountant's Compilation Report on Current-Period Financial Statements That Refers to a Predecessor Accountant's Compilation Report on Prior-Period Financial Statements

____

____

____

I (We) have compiled the accompanying balance sheet of ________________ [client name] as of ______________ [balance-sheet date], and the related statements of income and retained earnings and cash flows for the ________________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.[1]

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying 19__ [Current Year] financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

The 19__ financial statements of __________________ [client name] were compiled by other accountants whose report dated _____________, stated that they did not express an opinion or any other form of assurance on those statements.

[Signature]

[Date]

Note:

[1] This reporting guidance assumes that a combined statement of income and retained earnings is presented. If a separate statement of retained earnings is presented, the report should be worded as follows:

> I (We) have reviewed the accompanying balance sheet of __________________ [client name] as of ______________ [balance-sheet date] and the related statements of income, retained earnings, and cash flows for the ________________ [period] then ended,....

8.604 Successor Accountant's Compilation Report on Current-Period Financial Statements That Refers to a Predecessor Accountant's Review Report on Prior-Period Financial Statements

____

____

____

I (We) have compiled the accompanying balance sheet of ________________ [client name] as of ______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the _______________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying 19__ [Current Year] financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

The 19__ financial statements of ________________ [client name] were reviewed by other accountants whose report dated __________, stated that they were not aware of any material modifications that should be made to those statements in order for them to be in conformity with generally accepted accounting principles.

[Signature]

[Date]

8.605 Successor Accountant's Review Report on Current-Period Financial Statements That Refers to a Predecessor Accountant's Compilation Report on Prior-Period Financial Statements

____
____
____

I (We) have reviewed the accompanying balance sheet of ______________ [client name] as of ______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the ________________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of ________________[client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying 19__ [current year] financial statements in order for them to be in conformity with generally accepted accounting principles.

The 19__ financial statements of _________________________ [client name] were compiled by other accountants whose report dated ________________, stated that they did not express an opinion or any other form of assurance on those statements.

[Signature]

[Date]

8.606 Successor Accountant's Review Report on Current-Period Financial Statements That Refers to a Predecessor Accountant's Review Report on Prior-Period Financial Statements

____
____
____

I (We) have reviewed the accompanying balance sheet of ______________________ [client name] as of ______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the ________________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of ________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying 19__ [current year] financial statements in order for them to be in conformity with generally accepted accounting principles.

The 19__ financial statements of _________________________ [client name] were reviewed by other accountants whose report dated _________________, stated that they were not aware of any material modifications that should be made to those statements in order for them to be in conformity with generally accepted accounting principles.

[Signature]

[Date]

8.607 Continuing Accountant's Report on Comparative Statements — Both Periods Compiled

____
____
____

I (We) have compiled the accompanying balance sheets of ______________________ [client name] as of ______________ [balance-sheet dates], and the related statements of income and retained earnings, and cash flows for the ________________ [periods] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

8.608 Continuing Accountant's Report on Comparative Statements — Both Periods Reviewed

____

____

____

I (We) have reviewed the accompanying balance sheets of ______________________ [client name] as of ______________ [balance-sheet dates], and the related statements of income and retained earnings, and cash flows for the ________ [periods] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of _______________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) reviews, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

[Signature]

[Date]

8.609 Continuing Accountant's Report on Comparative Statements—Current Period Reviewed and Prior Period Compiled

____
____
____

I (We) have reviewed the accompanying balance sheet of ______________________ [client name] as of ______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the ________________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of _______________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying 19__ [current year] financial statements in order for them to be in conformity with generally accepted accounting principles.

The accompanying 19__ financial statements of ________________________ [client name] were compiled by me (us). A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the 19__ financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

8.610 Continuing Accountant's Report on Comparative Statements — Current Period Compiled with Reissued Review Report on Prior Period

____

____

____

I (We) have compiled the accompanying balance sheet of ______________________ [client name] as of ____________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the ______________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying 19__ [current year] financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

The accompanying 19__ financial statements of __________________________ [client name] were previously reviewed by me (us) in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in the 19__ financial statements is the representation of the management (owners) of ______________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying 19__ financial statements in order for them to be in conformity with generally accepted accounting principles. I (We) have not performed any review procedures since ______________ [original report date], the date of my (our) report on the accompanying 19__ financial statements.

[Signature]

[Date]

8.611 Continuing Accountant's Report on Comparative Statements — Current Period Compiled with Reference to Review Report on Prior Period

____
____
____

I (We) have compiled the accompanying balance sheet of ______________________ [client name] as of _______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the _______________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying 19__ [current year] financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

The accompanying 19__ financial statements of ________________________ [client name] were previously reviewed by me (us) and my (our) report dated ______________ [original report date], stated that I was (we were) not aware of any material modifications that should be made to those statements in order for them to be in conformity with generally accepted accounting principles. I (We) have not performed any procedures in connection with that review engagement after the date of my (our) report on the 19__ financial statements.

[Signature]

[Date]

8.612 Continuing Accountant's Report on Comparative Statements — Current Period Compiled with Reference to Audit Report on Prior Period

____
____
____

I (We) have compiled the accompanying balance sheet of ______________________ [client name] as of _______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the __________________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying 19__ [current year] financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

The financial statements for the __________________ [period] ended ______________________ [balance-sheet date], were audited by me (us) and I (we) expressed an unqualified opinion on them in my (our) report dated ________________ [original report date], but I (we) have not performed any auditing procedures since that date.

[Signature]

[Date]

8.613 Continuing Accountant's Report on Comparative Statements — Current Period Reviewed with Reference to Audit Report on Prior Period

____

____

____

I (We) have reviewed the accompanying balance sheet of ______________________ [client name] as of ______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the ________________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of _______________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying 19__ [current year] financial statements in order for them to be in conformity with generally accepted accounting principles.

The financial statements for the _______________ [period] ended ____________________ [balance-sheet date], were audited by me (us) and I (we) expressed an unqualified opinion on them in my (our) report dated _______________ [original report date], but I (we) have not performed any auditing procedures since that date.

[Signature]

[Date]

8.614 Continuing Accountant's Report on Comparative Statements — Both Periods Compiled with Substantially All Disclosures Omitted

____
____
____

I (We) have compiled the accompanying balance sheets of _______________________ [client name] as of _______________ [balance-sheet dates], and the related statements of income and retained earnings, and cash flows for the _________________ [periods] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the disclosures required by generally accepted accounting principles. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows. Accordingly, these financial statements are not designed for those who are not informed about such matters.

[Signature]

[Date]

8.615 Continuing Accountant's Compilation Report on Comparative Statements — Prior-Period Financial Statements Compiled with Substantially All Disclosures Omitted from Previously Reviewed Financial Statements

____
____
____

I (We) have compiled the accompanying balance sheets of ______________________ [client name] as of ______________ [balance-sheet dates], and the related statements of income and retained earnings, and cash flows for the ________________ [periods] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the disclosures required by generally accepted accounting principles. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows. Accordingly, these financial statements are not designed for those who are not informed about such matters.

The accompanying 19__ [prior year] financial statements were compiled by me (us) from financial statements that did not omit substantially all of the disclosures required by generally accepted accounting principles and that I (we) previously reviewed as indicated in my (our) report dated ______________ [original report date].

[Signature]

[Date]

8.616 Continuing Accountant's Report on Comparative Statements—Both Periods Compiled with Restatement of Prior-Period Financial Statements

____
____
____

I (We) have compiled the accompanying balance sheets of ________________________ [client name] as of _______________ [balance-sheet dates], and the related statements of income and retained earnings, and cash flows for the __________________ [periods] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

In my (our) previous compilation report dated _______________ [original report date], I (we) referred to a departure from generally accepted accounting principles because the Company carried its land at appraisal values. However, as disclosed in Note __, the Company has restated its 19__ financial statements to reflect its land at cost in accordance with generally accepted accounting principles.

[Signature]

[Date]

8.617 Continuing Accountant's Report on Comparative Statements — Current Period Compiled with Reference to Review Report on Restated Prior-Period Financial Statements

____
____
____

I (We) have compiled the accompanying balance sheet of ________________________ [client name] as of _______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the _________________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying 19__ [current year] financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

The accompanying 19__ financial statements of __________________________ [client name] were previously reviewed by me (us) and in my (our) report dated _____________ [original report date], I (we) referred to a departure from generally accepted accounting principles because the Company carried its land at appraisal values. However, as disclosed in Note __, the Company has restated its 19__ financial statements to reflect its land at cost in accordance with generally accepted accounting principles. I (We) have not performed any procedures in connection with that review engagement after the date of my (our) report on the 19__ financial statements.

[Signature]

[Date]

8.618 Reissued Predecessor Accountant's Review Report on Restated Prior-Period Financial Statements

____
____
____

I (We) have reviewed the accompanying balance sheet of ______________________ [client name] as of ______________ [balance-sheet date], and the related statements of income and retained earnings, and cash flows for the ________________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of ________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying 19__ financial statements in order for them to be in conformity with generally accepted accounting principles.

In my (our) previous review report dated ____________ [original report date], I (we) referred to a departure from generally accepted accounting principles because the Company carried its land at appraisal values. However, as disclosed in Note __, the Company has restated its 19__ financial statements to reflect its land at cost in accordance with generally accepted accounting principles.

[Signature]

____________________ [original report date],
except for Note ________, as to which the date
is ___________ [date of the event or revision]

Other Comprehensive
Bases of Accounting

CHAPTER 9

FINANCIAL STATEMENTS PREPARED ON ANOTHER COMPREHENSIVE BASIS OF ACCOUNTING

Table of Contents

Table of Contents (Continued)

CHAPTER 9

FINANCIAL STATEMENTS PREPARED ON ANOTHER COMPREHENSIVE BASIS OF ACCOUNTING

Table of Contents (Continued)

CHAPTER 9

FINANCIAL STATEMENTS PREPARED ON ANOTHER COMPREHENSIVE BASIS OF ACCOUNTING

9.000 APPLICABILITY OF SSARS

9.001 An accountant may be engaged to compile or review the financial statements of entity that prepares its statements on some other comprehensive basis of accounting (OCBOA). This possibility is specifically recognized in Statements on Standards for Accounting and Review Services (SSARS), as indicated by the following definition of a financial statement that is contained in SSARS No. 1:

> A presentation of financial data, including accompanying notes, derived from accounting records and intended to communicate an entity's economic resources or obligations at a point in time, or the changes therein for a period of time, in accordance with generally accepted accounting principles or a comprehensive basis of accounting other than generally accepted accounting principles.

Therefore, if an accountant submits an OCBOA financial statement to his or her client or others, the accountant should comply with the requirements of SSARS. (See sections 2.120 through 2.128 of Chapter 2 for a discussion of what constitutes submission of a financial statement.)

9.100 WHEN ARE OCBOA FINANCIAL STATEMENTS APPROPRIATE?

9.101 Professional standards do not address when it is appropriate to present financial statements in accordance with OCBOA. However, there are many circumstances in which OCBOA is as appropriate or more appropriate than generally accepted accounting principles. For example, financial statements prepared for partners in a limited partnership might be more appropriately presented on the tax basis of accounting then GAAP. Writing in *The Journal of Commercial Bank Lending*, Judith O'Dell, former chairperson of the Technical Issues Committee of the PCPS, has indicated that OCBOA financial statements can be efficient and appropriate for businesses meeting some or all of the following criteria:

- The business is managed by the owner who is closely involved in the day-to-day operations and financial aspects of the business.
- The business is a small, closely held business with little or no unsecured debt.
- The business has a cash flow that corresponds to its income and expenses.
- The company is not highly leveraged.

OCBOA financial statements would not be appropriate for businesses that:

- Anticipate going public.
- Have loan covenants requiring GAAP-basis financial statements.
- Have numerous absentee owners
- Have substantial unfunded obligations, commitments, and contingent obligations that would not be recorded on the tax or cash basis.

9.102 A 1990 survey of PCPS members indicated that OCBOA is most commonly used for businesses in the following industries:

- Professional services
- Medical
- Retail
- Real estate

9.200 WHAT ARE OTHER COMPREHENSIVE BASES OF ACCOUNTING?

9.201 An authoritative discussion of OCBOA is contained in Statements on Auditing Standards (SAS) No. 62, *Special Reports*. SAS No. 62 states that OCBOA includes only the following four categories of presentations:

- *Tax basis.* The basis of accounting that the reporting entity uses or expects to use to file its income tax return for the period covered by the financial statements (sections 9.205 through 9.208).
- *Cash/Modified cash basis.* The cash receipts and disbursements basis of accounting, and modifications of the cash basis having substantial support, such as recording depreciation on fixed assets or accruing income taxes (sections 9.209 through 9.213).
- *Other.* A definite set of criteria having substantial support that is applied to all material items appearing in financial statements, such as the price-level basis of accounting (sections 9.214 through 9.216).
- *Regulatory.* A basis of accounting that the reporting entity uses to comply with the requirements or financial reporting provisions of a governmental regulatory agency to whose jurisdiction the entity is subject; for example, the basis of accounting that insurance companies use pursuant to the rules of a state insurance commission (section 9.217).

9.202 In a 1994 survey of 2,000 members of the AICPA's Private Companies Practice Section (PCPS) the respondents indicated that 99% of the OCBOA statements their firms report on are on the cash, modified cash, and tax bases of accounting. The survey asked the members how, and to what extent, they apply current accounting and reporting literature to cash and tax basis statements, including information about presentation and disclosure issues. A nonauthoritative publication, *Preparing and Reporting on Cash- and Tax-Basis Financial Statements* was developed from the results of the survey. The guide includes a discussion of the key issues that arise when preparing and reporting on these statements, the results of the survey, and several sample financial statements submitted by the respondents.[1]

9.203 SAS No. 62 specifies certain bases that are not considered OCBOA. These include:

- Provisions of a loan agreement that require the borrower to prepare financial statements with assets, such as inventory, presented on a method of accounting that is not in accordance with generally accepted principles (GAAP) or OCBOA.
- Provisions of an acquisition agreement that require the preparation of financial statements that are in conformity with GAAP except for certain assets, such as receivables, inventories, or properties.

These types of presentations are considered special-purpose presentations. Refer to Chapter 12, section 12.206 for additional information.

9.204 If an accountant compiles or reviews financial statements that do not qualify as OCBOA, he or she should report on them as GAAP financial statements, pointing out all departures from GAAP in the compilation or review report. (See sections 10.306 through 10.307 of Chapter 10 for a discussion of reports on financial statements that contain departures from GAAP in prescribed forms, and sections 12.201 through 12.210 of Chapter 12 for a discussion of special reports prepared on a regulatory or contractual basis of accounting.)

The Income Tax Basis of Accounting

9.205 The income tax basis of accounting involves preparing financial statements based on the methods and principles that are used by the client to file its income tax return. Entities that typically use the income tax basis of accounting include small businesses for which conversion to GAAP is costly, and partnerships for which income tax basis financial statements provide the most useful information to the financial statement users.

9.206 Few additional guidelines need to be established for the income tax basis, because this method is based on Federal tax laws. However, one important issue is the treatment of nontaxable revenues and nondeductible expenses (i.e., interest income from municipal bonds and officers' life insurance premiums). In presenting financial statements on the income tax basis, nontaxable revenues and nondeductible expenses should be recognized in the financial statements when they are received or paid (for a cash basis taxpayer), or when they are accruable (for an accrual basis taxpayer).

9.207 **Additional Income Taxes for Prior Years.** Another issue that arises in the use of the tax basis is the treatment of income tax assessments that result from IRS examinations of prior years' tax returns. Appropriate methods of handling these assessments are described below:

- The amount may be charged to expense in the current period if there are no corresponding adjustments to the balance sheet for expenses capitalized or revenue recognized.

---

[1] To obtain a copy of this publication, call the AICPA Order Department at 800-862-4272 and ask for product no. 006700. ($35 AICPA members, $38.50 non-members.)

- The amount may be treated as a prior-period adjustment and charged to retained earnings if the assessment affects balance sheet amounts (e.g., by requiring disallowed expenses to be capitalized and amortized, or by requiring recognition of previously unreported revenue).

The method used should be disclosed.

9.208 Accounting Changes for Tax Purposes. The effects of accounting changes are often recognized prospectively over a specified number of years for tax purposes. For financial reporting purposes, the accounting change should be treated in the same manner as it is treated in the tax return.

The Cash Basis of Accounting

9.209 The cash basis of accounting consists of recording transactions on the basis of cash receipts and disbursements. Using this method of accounting, certain revenues are recognized when the cash is received rather than when the revenues are earned, and certain expenses are recognized when they are paid rather than when the obligations are incurred. Entities typically use the cash basis of accounting when conversion to GAAP is costly.

9.210 Pure Cash Basis. Under the "pure" cash basis, long-term assets are not capitalized so there is no depreciation or amortization. Accruals are not made and prepaid assets are not recorded. Under this basis, the statement of assets and liabilities would include only cash and owner's equity. Pure cash-basis financial statements may be appropriate for certain smaller companies when cash flow is of primary importance to management and a limited number of users. Examples of some entities that may use the pure cash basis of accounting include:

- Estates and trusts
- Civic ventures
- Student activity funds

9.211 Modified Cash Basis. The cash basis is usually accompanied by certain modifications that have substantial support. A modification has substantial support if the method is equivalent to the accrual basis of accounting for the item and if use of the method is not illogical. For example, it would be illogical to record revenue on the accrual basis and expenses on the cash basis. SAS No. 62 makes reference to only two modifications as having substantial support: depreciation on fixed assets and accruing income taxes. Clearly, other modifications that can be considered to have substantial support have evolved through common usage and practice.

9.212 The 1994 survey of PCPS members indicated that the following are the most typical cash basis modifications:

- Capitalizing expenditures for property, plant and equipment
- Recording depreciation expense and accumulated depreciation
- Recording liabilities for short-term and long-term borrowings
- Capitalizing expenditures for inventory

9.213 Writing in *The CPA Journal*, Wayne Bremser and Kenneth Hiltebeitel identify some possible cash-basis modifications that are normally considered as "the last level of adjustment to bring statements to GAAP basis or GAAP basis with a departure(s)."[2] These possible adjustments are:

- Accounts receivable and unpaid purchases
- Deferred income taxes and deferred tax expense
- Capital lease assets and obligations under capital leases

Using this logic, if a set of financial statements included one of these three modifications, that may be an indication that they are equivalent to GAAP basis with a departure(s).

A Definite Criterion Applied to Items in the Financial Statements

9.214 This category of OCBOA is somewhat controversial. The only definitive example is price-level adjusted financial statements. However, many accountants believe that this category also provides a basis for the use of the estimated current value (or cost) method of accounting. Other accountants believe that there are too many variations in methods of determining current value information for it to constitute OCBOA. For example, the following methods have been used to determine the estimated current values of assets and liabilities:

- Current market value (i.e., sales value less costs of disposal)
- Current replacement cost
- Discounted future cash receipts and payments

9.215 An interpretation of SAS No. 62 titled *Reporting on Current-Value Financial Statements That Supplement Historical-Cost Financial Statements in a General-Use Presentation of Real Estate Entities* (AU 9623.55-.59) implies that current-value financial statements are not appropriate for general use unless they are presented as a supplement to historical financial statements. Therefore, the authors recommend that the current value **not** be regarded as another comprehensive basis of accounting.

Practice Tip:

Generally accepted accounting principles require the use of the current value basis of accounting for certain entities, such as investment companies, employee benefit plans, personal financial statements, and mutual and common trust funds.

---

[2] "A Look At The Modified Cash Basis," by Wayne G. Bremser, Ph.D., CPA and Kenneth M. Hiltebeitel, Ph.D., CPA, *The CPA Journal*, February, 1992.

9.216 Occasionally, the questions arises as to whether some other basis of accounting that differs from GAAP can be considered an OCBOA. Respondents to the 1994 PCPS survey indicated that 99 percent of the OCBOA statements they report on are on the cash, modified cash, and tax bases of accounting. In other words, the respondents seemed to indicate that they consider these three bases — and virtually no others — to meet the "substantial support" criterion. The authors therefore believe that, rather than question whether some other accounting basis can be considered OCBOA, practitioners are well-advised to stay within the bases of accounting currently viewed as having substantial support.

The Regulatory Basis of Accounting

9.217 Financial statements prepared on a regulatory basis should generally be limited to those that are filed with the applicable regulatory agency. When the entity prepares financial statements that are to be used by creditors or other external users, the financial statements generally should be prepared on a cash/modified cash, tax, or GAAP basis.

9.300 PRESENTATION OF OCBOA FINANCIAL STATEMENTS

9.301 This section describes the presentation guidelines for the most commonly used OCBOA financial statements — financial statements presented on the income tax basis of accounting, and financial statements presented on the modified cash basis of accounting.

Titles of OCBOA Financial Statements

9.302 The titles used for OCBOA financial statements are important. They should be descriptive of the accounting basis being used and avoid the implication that the financial statements are presented in accordance with GAAP. SAS No. 62 precludes the use of unmodified GAAP-basis titles for OCBOA statements. The literature is silent, however, as to the use of unmodified GAAP-basis captions within the statements. Some practitioners believe the captions used within the financial statements should be modified because they are associated with GAAP-basis financial statements, while others do not believe modification of the captions is necessary. Examples of modified captions that can be used include "net income — cash basis" and "retained earnings — cash basis" or "excess of revenue collected over expenses paid" and "accumulated excess of revenue collected over expenses paid." Illustration 9-1 includes examples of commonly used titles for financial statements presented on the income tax, modified cash, and "pure" cash bases of accounting.

Statement of Cash Flows

9.303 When a set of financial statements purport to present financial position and results of operations in accordance with GAAP, SFAS No. 95, *Statement of Cash Flows*, requires presentation of a statement of cash flows. It is generally understood that the phrase "financial position and results of operations" refers to a GAAP presentation. Because OCBOA financial statements do not purport to present financial position and results of operations in accordance with GAAP, presentation of a statement of cash flows for tax or cash basis financial statements is optional. In the 1994 survey of PCPS members, half of the respondents indicated that they include a statement of cash flows with financial statements presented on a modified cash or tax basis. In deciding whether a statement of cash flows is included, these respondents indicated that they consider:

- *The type of financial statements*. Practitioners are more likely to include a statement of cash flows in tax basis financial statements or in modified cash basis financial statements when the modifications create material differences between revenue and expenses and cash flows.
- *Understandability and usefulness*. Practitioners are more likely to include a statement of cash flows when it is considered to be understandable and relevant to management and other users.

Practice Tip:

An entity that changes its presentation from a cash (or income tax) basis to the accrual basis (or vice versa), should account for the change as a prior-period adjustment. Prior-period financial statements presented in comparative form should be restated to the accrual basis, with the cumulative effect of the change reported as an adjustment to beginning retained earnings of the earliest year presented. If only the current year's statements are presented, the cumulative effect of the change should be reported as an adjustment to beginning retained earnings. In both cases, the change in accounting basis should be disclosed in the notes to the financial statements.

Illustration 9-1

OCBOA Financial Statement Titles

Income Tax Basis

Statement of Assets and Liabilities — Income Tax Basis
Statement of Revenues and Expenses (and Retained Earnings) — Income Tax Basis
or
Balance Sheet — Income Tax Basis
Statement of Income — Income Tax Basis

Modified Cash Basis

Statements of Assets and Liabilities — Modified Cash Basis
Statement of Revenues and Expenses (and Retained Earnings) — Modified Cash Basis
or
Statement of Assets and Liabilities Arising from Cash Transactions
Statement of Revenues Collected and Expenses Paid

Cash Basis

Statement of Assets and Owners' Equity — Cash Basis
Statement of Cash Receipts and Disbursements — Cash Basis

Disclosures in OCBOA Financial Statements

9.304 A common misconception about OCBOA financial statements is that the requirements for disclosure are different from those for GAAP financial statements. This is not the case. The advantage of adopting tax or cash basis financial statements lies in the measurement differences. For example, in cash and tax-basis financial statements capital leases and deferred taxes don't have to be presented, and receivables and payables may not have to be accrued.

9.305 SAS No. 62 makes it clear that disclosures in OCBOA financial statements are similar to those contained in GAAP financial statements. Footnote No. 4 of SSARS No. 1 states that SAS No. 62 disclosure requirements should be followed for compiled or reviewed OCBOA financial statements.

9.306 SAS No. 62 allows for considerable judgment in the nature and extent of OCBOA financial statement disclosures; however, it provides the following guidelines:

- OCBOA financial statements should include a **summary of significant accounting policies** that discusses the basis of presentation and describes how it differs from GAAP.
- If OCBOA financial statements include items that are the same as or similar to those in GAAP statements, **similar informative disclosures** are appropriate.
- Matters that are **not specifically identified on the face of the financial statements** should be considered for disclosure. These items include: related party transactions, restrictions on assets and owners' equity, subsequent events, and uncertainties.

The authors strongly urge you to carefully read paragraphs .09 and.10 of SAS No. 62, which discuss the disclosure guidance summarized above.

9.307 The 1994 PCPS Survey asked practitioners to indicate the frequency with which they made certain disclosures.

In general, the respondents indicated they were **most likely** to include disclosures about the following items:

- Terms of debt agreements and future minimum payments
- Terms of leases and future minimum payments
- Information about defined benefit and defined contribution pension plans
- Commitments and contingencies
- Going-concern uncertainties

The respondents **sometimes** include disclosures about:

- Off-balance sheet risk and concentration of credit risk
- Income taxes

They were **least likely** to include disclosures about:

- Fair value of financial instruments
- Postretirement and postemployment benefits
- For common interest realty associations (CIRAs), disclosures related to future major repairs and replacements

9.308 The Survey also asked the respondents to comment on the factors they considered in determining whether to include certain disclosures. In general, those factors included the following:

- *Relevancy, usefulness, understandability*. If the information was judged to be important to the users, it was more likely to be disclosed. Information about commitments and contingencies was generally perceived to be more relevant and easier to understand than information about fair value of financial instruments. Client circumstances may make certain information less relevant. For example, if the financial statements had a distribution limited to the geographic area where an entity does all its business, information about geographic concentrations of credit risk may not have been considered relevant.

- *Cost/benefit.* Information that was costly to obtain was less likely to be disclosed unless the benefits of disclosure clearly outweighed the cost.
- *Inclusion of the item in the financial statements.* Accountants were more likely to disclose information related to specific items that were recognized in the financial statements than to disclose "off-balance-sheet information," such as concentration of credit risk.

Section 9.400 of this chapter contains examples of modified cash and tax basis financial statements that include many of these disclosures, and section 14.700 presents a "Disclosure Checklist for Financial Statements Prepared on Another Comprehensive Basis of Accounting (Tax or Cash Basis)."

9.309 Disclosure of the Basis of Accounting. As indicated above, OCBOA financial statements should include a "Summary of Significant Accounting Policies." This note should disclose the following:

- The basis of accounting.
- The ways in which revenues and expenses and related assets and liabilities are recognized.
- A description of how the basis of accounting differs from GAAP, but the effects of the differences need not be quantified.
- In interim financial statements, the disclosure should include information about interim estimates — for example, how inventories and cost of goods sold were estimated.

9.310 When the accountant is reporting on compiled OCBOA financial statements that omit substantially all disclosures, including the basis of accounting, SSARS No. 1, paragraph 20 requires that the basis of accounting be disclosed in the accountant's report. For example, the following sentence could be added to the first paragraph of the standard compilation report:

> The financial statements have been prepared on the accounting basis used by the Company for federal income tax purposes, which is a comprehensive basis of accounting other than generally accepted accounting principles.

9.311 Disclosure of Risks and Uncertainties. SOP 94-6, *Disclosure of Certain Significant Risks and Uncertainties*, is effective for calendar year 1995 and applies to all nongovernmental entities whose financial statements are prepared in accordance with GAAP. The Statement requires that all entities disclose nature of operations and the fact that estimates are used in the preparation of the financial statements. It also requires that entities meeting certain conditions should disclose certain significant estimates and current vulnerability due to certain concentrations. The requirements of the Statement are described in further detail in Chapter 1, sections 1.610-1.625.

9.312 When it comes to applying GAAP disclosure requirements to OCBOA statements, SOP 94-6 is no different from other pronouncements. It is highlighted in this chapter because its requirements are new for 1995 and there are differences of opinion as to how the requirements relate to OCBOA statements. Many practitioners believe that they apply while others believe they do not. SAS No. 62, paragraph 10 indicates that accountants should consider disclosure of uncertainties. Therefore, as with most other GAAP disclosure requirements, accountants preparing or reporting on OCBOA statements should rely on their judgment as to whether SOP 94-6 disclosures are useful to the financial statement users.

9.313 For OCBOA statements, it certainly seems appropriate to disclose a description of the nature of operations and the fact that estimates are used in the preparation of financial statements. But should certain significant estimates or vulnerability to concentrations be disclosed? Consider the following example:

> Conglomerated Construction Co. uses a particular building material on most of its projects. At year-end, management has become aware of the fact that it is reasonably possible that there will be a shortage in this crucial material (assume that it cannot be substituted) in the next few months. The shortage is expected to result in a significant price increase that the Company will be unable to pass along to its customers. The price increase is expected to have a severe impact on the financial condition of the Company.

9.314 For GAAP statements, this situation must be disclosed in accordance with SOP 94-6. For OCBOA statements, the accountant must apply his or her judgment to determine whether such disclosure is useful. In other words, would the financial statements be informative of all matters affecting their use if this situation was not disclosed? For this example, the authors consider disclosure of this situation important and informative and would include it in OCBOA statements. The authors recommend that accountants focus on the informative nature of such disclosures to the users of the financial statements when considering whether certain estimates or concentrations should be disclosed in OCBOA statements.

9.400 ILLUSTRATIVE FINANCIAL STATEMENTS

9.401 This section includes examples of financial statements prepared on the modified cash (section 9.402) and the income tax bases of accounting (section 9.403).

Sample OCBOA
Financial Statements

9.402 Illustrative Financial Statements—Modified Cash Basis

Warren Corporation
Statements of Assets and Liabilities—Modified Cash Basis
December 31, 19X2 and 19X1

	19X2	19X1
ASSETS		
Current Assets		
Cash	$ 53,000	$ 18,600
Due from officer (Note 2)	—	45,000
Total Current Assets	53,000	63,600
Property and equipment, at cost (Note 1)		
Furniture	73,000	64,000
Office equipment	52,000	48,000
Leasehold improvements	72,000	72,000
	197,000	184,000
Less: Accumulated depreciation and amortization (Note 1)	67,000	42,000
	130,000	142,000
Total Assets	$ 183,000	$ 205,600
LIABILITIES		
Current Liabilities		
Loan payable to bank, current portion (Note 3)	$ 16,000	$ 16,000
Note payable to officer (Note 2)	30,000	—
Total Current Liabilities	46,000	16,000
Loan payable to bank (Note 3)	103,000	119,000
Total Liabilities	149,000	135,000
STOCKHOLDERS' EQUITY		
Common stock, $1.00 par value, authorized 10,000 shares, issued and outstanding 5,000 shares	5,000	5,000
Additional paid-in capital	15,000	15,000
Retained earnings	14,000	50,600
Total Stockholders' Equity	34,000	70,600
Total Liabilities and Stockholders' Equity	$ 183,000	$ 205,600

See the accompanying notes and accountant's report.

Warren Corporation
Statements of Revenues and Expenses
and Retained Earnings — Modified Cash Basis
for the Years Ended December 31, 19X2 and 19X1

	19X2	19X1
REVENUES		
Operating revenues	$ 1,015,900	$ 1,105,000
Miscellaneous	3,000	6,500
	1,018,900	1,111,500
EXPENSES		
Salaries and bonuses	920,000	954,000
Advertising	8,000	7,400
Rent (Note 4)	87,000	82,000
Depreciation and amortization (Note 1)	25,000	22,000
State and local income taxes paid	8,000	10,000
Federal income taxes paid (Notes 1 and 5)	1,500	7,500
Other expenses paid	6,000	8,300
	1,055,500	1,091,200
Net income (loss)	(36,600)	20,300
RETAINED EARNINGS		
Balance, beginning of year	50,600	30,300
Balance, end of year	$ 14,000	$ 50,600

See accompanying notes and accountant's report.

Warren Corporation
Notes to Financial Statements — Modified Cash Basis

Note 1 — Summary of Significant Accounting Policies

The Company prepares its financial statements on the cash basis but includes depreciation and amortization of capitalized assets. Under this basis, revenues are recognized when collected rather than when earned, and expenses are recognized when paid rather than when incurred. Consequently, accounts receivable due from customers, amounts due vendors and suppliers, and the unpaid portion of taxes at December 31, 19X2 and 19X1, are not included in the financial statements.

If an expenditure results in an asset having an estimated useful life that extends beyond the year of acquisition, the expenditure is capitalized. Furniture, office equipment, and leasehold improvements are recorded at cost. Depreciation on furniture and office equipment is provided on the straight-line method over the estimated useful lives of the assets. Amortization of leasehold improvements is provided on the straight-line method over the term of the lease or the estimated useful lives of the improvements, whichever is shorter.

Income taxes are recognized as an expense when paid.

Note 2 — Transactions with Related Parties

At December 31, 19X1, Bill Warren, the Company's president, owed $45,000 to the Company. This amount was repaid with interest at 10 percent per annum. During 19X2, the Company borrowed $30,000 from Linda Ward, the Company's Treasurer in exchange for a promissory note due November 30, 19X3, bearing interest at 10 percent per annum.

Note 3 — Loan Payable to Bank

The loan payable to bank consisted of the following:

	December 31,	
	19X2	19X1
Loan payable to bank due in quarterly installments of $4,000 until December 31, 19Y2, plus interest at 12%	$119,000	$135,000
Less: Current maturities	(16,000)	(16,000)
Long-term portion	$103,000	$119,000

The loan matures in the next five years as follows:

19X3	$16,000
19X4	$16,000
19X5	$16,000
19X6	$16,000
19X7	$16,000

Note 4 — Leases

The Company leases office space and certain data processing and other equipment under leases for varying terms. At December 31, 19X2, the minimum rental payments under noncancellable leases with a term in excess of one year were as follows:

19X3	$84,000
19X4	$84,000
19X5	$84,000
19X6	$78,000
19X7	$78,000

Note 5 — Contingencies

The Company is a defendant in a legal action alleging breach of contract in which the plaintiff is seeking damages of $75,000. In the opinion of the Company's legal counsel, this matter is not expected to result in an award that would have a materially adverse effect on the Company's financial position.

The Internal Revenue Service has examined the Company's income tax returns through 19X0, or the period during which such returns could be examined has expired. No examinations were under way or completed during 19X2.

9.403 Illustrative Financial Statements — Income Tax Basis

Terra Nova Partnership Ltd.
Statement of Assets and Liabilities — Income Tax Basis
December 31, 19X2

ASSETS	
Current Assets	
Cash	$ 64,800
Property and equipment, at cost (Note 3)	
Rental apartments	4,120,000
Furniture and equipment	17,900
	4,137,900
Less: Accumulated depreciation (Note 3)	(145,400)
	3,992,500
Total Assets	$4,057,300
LIABILITIES AND PARTNERS' CAPITAL	
Current Liabilities	
Rental deposits	$ 30,000
Current portion of mortgage payable (Note 4)	38,500
Total Current Liabilities	68,500
Mortgage payable (Note 4)	2,777,500
Total Liabilities	2,846,000
Partners' Capital	1,211,300
Total Liabilities and Partners' Capital	$4,057,300

See accompanying notes and accountant's report.

Terra Nova Partnership Ltd.
Statement of Revenues and Expenses and
Partners' Capital — Income Tax Basis
for the Year Ended December 31, 19X2

REVENUE	
Rental	$ 654,500
Interest income	350
	654,850
EXPENSES	
Salaries	72,400
Repairs, maintenance and cleaning	27,000
Insurance	15,000
Real estate taxes	76,000
Utilities	8,700
Interest	288,000
Depreciation and amortization (Note 3)	180,000
Miscellaneous	6,500
	673,600
Excess of Expenses Over Revenues	(18,750)
Partners' Capital at Beginning of Year	1,230,050
Partners' Capital at End of Year	$1,211,300

See accompanying notes and accountant's report.

Terra Nova Partnership Ltd.
Notes to the Financial Statements — Income Tax Basis

Note 1 — Partnership Activities

The partnership was formed in 19W6 to construct and operate a 112-unit apartment complex in Phoenix, Arizona.

Note 2 — Summary of Significant Accounting Policies

The accompanying financial statements have been prepared on the basis of accounting used for federal income tax purposes. Consequently, certain expenses are recognized in the determination of income in different reporting periods than they would be if the financial statements were prepared in conformity with generally accepted accounting principles.

Note 3 — Property and Equipment

Property and equipment are recorded at cost including interest charges on the loan to finance construction of the apartment complex. Depreciation is based on the modified accelerated cost recovery system. Recovery periods range from 5 to 27½ years.

Note 4 — Mortgage Payable

The mortgage payable is to North City Savings and Loan in monthly installments of $26,400 of principal and interest until December 1, 19Y8. Principal is payable for the next five years as follows:

19X3	$38,500
19X4	$41,300
19X5	$43,000
19X6	$46,100
19X7	$50,000

Note 5 — Income Taxes

The partnership is not subject to income taxes as a separate entity. The income tax effect of income and losses is passed through to the individual partners. Consequently, the partnership's excess expenses over revenues is presented without income tax benefit to the partnership.

Sample Reports — OCBOA

9.500 SAMPLE OCBOA REPORTS

9.501 The following pages include illustrative reports for various types of engagements involving OCBOA financial statements.

9.502 The illustrative reports in this chapter contain the SSARS No. 7 wording.

9.503 Compilation Report — Income Tax Basis, Standard Report

____
____
____

I (We) have compiled the accompanying statement of assets, liabilities and equity — income tax basis of ____________________ [client name] as of _______________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—income tax basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

9.504 Compilation Report — Income Tax Basis, Lack of Independence

____
____
____

I (We) have compiled the accompanying statement of assets, liabilities and equity — income tax basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—income tax basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

I am (We are) not independent with respect to ____________________ [client name].

[Signature]

[Date]

9.505 Compilation Report — Income Tax Basis, Substantially All Disclosures Omitted, Basis of Accounting Disclosed in the Financial Statements

____

____

____

I (We) have compiled the accompanying statement of assets, liabilities and equity — income tax basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—income tax basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the disclosures ordinarily included in financial statements prepared on the income tax basis of accounting. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's assets, liabilities, equity, revenue, and expenses. Accordingly, these financial statements are not designed for those who are not informed about such matters.

[Signature]

[Date]

9.506 Compilation Report — Income Tax Basis, Substantially All Disclosures Omitted, Basis of Accounting Not Disclosed in the Financial Statements

____

____

____

I (We) have compiled the accompanying statement of assets, liabilities and equity — income tax basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—income tax basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. The financial statements have been prepared on the accounting basis used by the Company for federal income tax purposes, which is a comprehensive basis of accounting other than generally accepted accounting principles.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the disclosures ordinarily included in financial statements prepared on the income tax basis of accounting. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's assets, liabilities, equity, revenue, and expenses. Accordingly, these financial statements are not designed for those who are not informed about such matters.

[Signature]

[Date]

9.507 Compilation Report — Income Tax Basis, Financial Statements Accompanied by Supplementary Information

____
____
____

I (We) have compiled the accompanying statement of assets, liabilities and equity — income tax basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—income tax basis for the year then ended, and the accompanying ______________________ [identify the supplementary information], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements and supplementary schedules information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and supplementary schedules and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

9.508 Compilation Report — Income Tax Basis, Statement of Assets, Liabilities and Equity Only

____
____
____

I (We) have compiled the accompanying statement of assets, liabilities and equity — income tax basis of ____________________ [client name] as of ________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statement and, accordingly, do not express an opinion or any other form of assurance on it.

[Signature]

[Date]

9.509 Compilation Report — Cash Basis, Standard Report

____
____
____

I (We) have compiled the accompanying statement of assets and liabilities — cash basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—cash basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

9.510 Compilation Report — Cash Basis, Lack of Independence

____
____
____

I (We) have compiled the accompanying statement of assets and liabilities — cash basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—cash basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

I am (We are) not independent with respect to ____________________ [client name].

[Signature]

[Date]

9.511 Compilation Report—Cash Basis, Substantially All Disclosures Omitted, Basis of Accounting Disclosed in the Financial Statements

____
____
____

I (We) have compiled the accompanying statement of assets and liabilities — cash basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—cash basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the disclosures ordinarily included in financial statements prepared on the cash basis of accounting. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's assets, liabilities, equity, revenue, and expenses. Accordingly, these financial statements are not designed for those who are not informed about such matters.

[Signature]

[Date]

9.512 Compilation Report—Cash Basis, Substantially All Disclosures Omitted, Basis of Accounting Not Disclosed in the Financial Statements

____

____

____

I (We) have compiled the accompanying statement of assets and liabilities — cash basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—cash basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. The financial statements have been prepared on the cash basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the disclosures ordinarily included in financial statements prepared on the cash basis of accounting. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's assets, liabilities, equity, revenue, and expenses. Accordingly, these financial statements are not designed for those who are not informed about such matters.

[Signature]

[Date]

9.513 Compilation Report — Cash Basis, Financial Statements Accompanied by Supplementary Information

____

____

____

I (We) have compiled the accompanying statement of assets and liabilities — cash basis of ____________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—cash basis for the year then ended, and the accompanying _______________________ [identify the supplementary information], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements and supplementary schedules information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and supplementary schedules and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

9.514 Compilation Report — Cash Basis, Statement of Assets and Liabilities Only

____

____

____

I (We) have compiled the accompanying statement of assets and liabilities — cash basis of ____________________ [client name] as of ________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statement and, accordingly, do not express an opinion or any other form of assurance on it.

[Signature]

[Date]

9.515 Review Report — Income Tax Basis, Standard Report

____
____
____

I (We) have reviewed the accompanying statement of assets, liabilities and equity — income tax basis of ________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—income tax basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of ____________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the income tax basis of accounting, as described in Note ___.

[Signature]

[Date]

9.516 Review Report — Income Tax Basis, Financial Statements Accompanied by Supplementary Information Covered by the Accountant's Review Procedures

____

____

____

I (We) have reviewed the accompanying statement of assets, liabilities and equity — income tax basis of ________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—income tax basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of ____________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the income tax basis of accounting, as described in Note ___.

The accompanying supplementary information contained in ________________ [identify the supplementary information] is presented only for supplementary analysis purposes and has been subjected to the inquiry and analytical procedures applied in the review of the basic financial statements. This information is presented on the income tax basis of accounting. I (We) did not become aware of any material modifications that should be made to the information.

[Signature]

[Date]

9.517 Review Report — Income Tax Basis, Statement of Assets and Liabilities Only

____

____

____

I (We) have reviewed the accompanying statement of assets, liabilities and equity — income tax basis of ________________ [client name] as of ________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this financial statement is the representation of the management (owners) of _____________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statement in order for it to be in conformity with the income tax basis of accounting, as described in Note ___.

[Signature]

[Date]

9.518 Review Report — Cash Basis, Standard Report

____

____

____

I (We) have reviewed the accompanying statement of assets and liabilities -- cash basis of ________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—cash basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of ____________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the cash basis of accounting, as described in Note ___.

[Signature]

[Date]

9.519 Review Report — Cash Basis, Financial Statements Accompanied by Supplementary Information Covered by the Accountant's Review Procedures

____

____

____

I (We) have reviewed the accompanying statement of assets and liabilities — cash basis of ________________ [client name] as of ________________ [financial statement date], and the related statement(s) of revenue and expenses (and retained earnings)—cash basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of ____________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the cash basis of accounting, as described in Note ___.

The accompanying supplementary information contained in _______________ [identify the supplementary information] is presented only for supplementary analysis purposes and has been subjected to the inquiry and analytical procedures applied in the review of the basic financial statements. This information is presented on the cash basis of accounting. I (We) did not become aware of any material modifications that should be made to the information.

[Signature]

[Date]

9.520 Review Report — Cash Basis, Statement of Assets and Liabilities Only

____
____
____

I (We) have reviewed the accompanying statement of assets and liabilities — cash basis of ________________ [client name] as of ________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this financial statement is the representation of the management (owners) of ______________________ [client name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statement in order for it to be in conformity with the cash basis of accounting, as described in Note ___.

[Signature]

[Date]

Prescribed Forms

CHAPTER 10

FINANCIAL STATEMENTS INCLUDED IN PRESCRIBED FORMS

Table of Contents

CHAPTER 10

FINANCIAL STATEMENTS INCLUDED IN PRESCRIBED FORMS

Table of Contents (Continued)

CHAPTER 10

FINANCIAL STATEMENTS INCLUDED IN PRESCRIBED FORMS

10.000 SPECIAL PROVISIONS FOR PRESCRIBED FORMS

10.001 Various bodies may design or adopt standard preprinted forms that require specific financial information about another entity. Banks, credit agencies, industry trade associations, and governmental and regulatory agencies are common examples of bodies that use such forms. Because these forms are designed to meet the specific requirements of the bodies using them, they often call for departures from generally accepted accounting principles (GAAP). Such departures may pertain to measurement principles not in conformity with GAAP, such as using appraised value instead of cost. These departures may also pertain to the failure to request disclosures required by GAAP, such as not requiring disclosure of commitments or contingencies.

10.002 Under the reporting requirements in Statement on Standards for Accounting and Review Services (SSARS) No. 1, GAAP or other comprehensive bases of accounting (OCBOA) departures must be disclosed in the accountant's compilation report. However, SSARS No. 3 provides an alternative form of compilation report on financial statements included in prescribed forms. The essence of this provision is elimination of the requirement to describe GAAP departures in the accountant's compilation report *for those departures required by the prescribed form.* The rationale underlying this provision is the presumption that the information required by a prescribed form is sufficient to meet the needs of the body that designed or adopted the form and that there is no need for the accountant to advise that body of GAAP departures required by the form.

10.003 The alternative report allowed by SSARS No. 3 is an option. The accountant may always elect to follow the reporting requirements in SSARS No. 1 and disclose all GAAP departures, including those called for by the prescribed form.

10.004 The reporting alternative for prescribed forms is available only for a compilation service. There is no provision for an alternative review report. If financial statements in a prescribed form are reviewed, all material GAAP departures, including those called for by the form, must be disclosed in the accountant's review report.

10.100 WHAT IS A PRESCRIBED FORM?

10.101 To be eligible for the reporting provision of SSARS No. 3, a prescribed form must have the following characteristics:

- *Preprinted* — The form must be preprinted. A set of instructions alone setting forth how financial statements are to be prepared would not, therefore, constitute a prescribed form.
- *Designed or Adopted by User* — The form must be one that the user of the financial statements has designed or selected for its use. A form designed or adopted by the entity whose financial statements are being compiled is not a prescribed form.
- *Call for GAAP Departures* — The form must call for departures from GAAP or OCBOA. A form that does not call for such departures, even if it has the other characteristics, is not a prescribed form for purposes of SSARS No. 3.
- *Not Pertaining to Sale or Trading of Securities of the Entity Submitting the Form* — A form that pertains to the sale or trading of the entity's own securities does not meet the definition of a prescribed form. However, some forms do not pertain to the sale or trading of the entity's own securities and these forms are considered to be prescribed forms for purposes of SSARS No. 3. Nonpublic broker-dealers, for example, may be required to submit prescribed forms to a stock exchange as part the exchange's regulation of the broker-dealer.
- *Not a Tax Return* — Although a tax return is a preprinted form designed by the body using the financial information, it is not a prescribed form. SSARS No. 1, paragraph 4, states that tax returns are not considered to be financial statements and, therefore, are already exempt from SSARS No. 1 requirements.

Medicare Cost Reports

10.102 As discussed in Chapter 2, sections 2.114 through 2.119, practice is diverse in its treatment of financial information in Medicare cost reports. The AICPA Accounting and Review Services Committee has issued no official guidance on this matter, but in 1994, the Committee took the position that such financial information meets the definition of a financial statement. Therefore, the accountant should comply with SSARS No. 1 when submitting such Medicare cost reports.

10.200 WHAT IS THE SSARS NO. 3 ALTERNATIVE?

10.201 When an accountant compiles financial statements in a prescribed form, he or she may elect to use a report that differs from the one required by SSARS No. 1. This alternative report is not required to disclose any departures from GAAP or OCBOA that are required by the prescribed form. (See section 10.703 for an illustrative report.)

Other Requirements in a SSARS No. 3 Engagement

10.202 SSARS No. 3 provides *only* a reporting alternative concerning GAAP departures required by the prescribed form. The accountant is not exempt from the other reporting and performance requirements established by SSARS No. 1 and SSARS No. 2. Thus, even when the accountant elects to use the SSARS No. 3 report alternative, he or she must nevertheless adhere to the following requirements:

- Establish an understanding with the client regarding the services to be performed and the report the accountant expects to render.

- Have or obtain a knowledge of the accounting principles and practices of the client's industry and a general understanding of certain matters related to the client itself.
- Consider whether it will be necessary to perform other accounting services, such as assistance in adjusting the books of account or consultation on accounting matters.
- Take certain actions when the accountant becomes aware that information supplied by the client is incorrect, incomplete, or otherwise unsatisfactory.
- Read the compiled financial statements and consider whether they appear to be in appropriate form and free from obvious material misstatement.
- Consider whether to modify the report if the accountant becomes aware of a material departure from either (1) GAAP or OCBOA that is *not* required by the prescribed form or (2) the requirements of the prescribed form.
- Mark each page of the prescribed form "See Accountant's Compilation Report."
- Modify the report if the accountant is not independent.
- Indicate in the report the responsibility, if any, the accountant assumes for any supplementary information presented.
- Follow guidance for reporting on comparative financial statements in SSARS No. 2.

10.203 Although the performance and reporting requirements listed in section 10.202 must be followed even when the accountant elects to use the SSARS No. 3 report alternative, they may need to be modified to fit a prescribed-form engagement. For example, the understanding with the client should include an indication that the accountant will use the SSARS No. 3 report alternative. The need to perform other accounting services might relate to services necessary to compile financial statements that meet the requirements of the prescribed form, such as obtaining appraisal values for certain assets. Reading the financial statements would be done from the perspective of the prescribed form requirements.

Signing a Preprinted Report

10.204 A prescribed form may contain a preprinted report that the accountant is requested to sign. The accountant should sign such a report only if its language conforms (or can be easily modified to conform) with the requirements of SSARS No. 3. In all other situations, the accountant should not sign the form, but should issue a separate report in accordance with SSARS No. 3. In the place on the form where the signature is requested, the accountant may include the following reference:

See the Accountant's Compilation Report.

Financial Statements Submitted Electronically

10.205 A regulatory agency or other user of financial statements may require that financial statements be submitted on a prescribed form using an electronic format. If the electronic form is designed without any way for the accountant to include a compilation report, the accountant should submit, separately, a printed copy of the financial statements and compilation report to the requesting party.

10.300 REPORTING ON DEPARTURES IN A PRESCRIBED FORM

10.301 As noted in section 10.201, the accountant who elects to use the SSARS No. 3 report alternative is not required to disclose in the compilation report any GAAP or OCBOA departures that are called for by the prescribed form. Other departures, however, must be disclosed in the report when they are material. These departures fall into two categories —

1. Departures from GAAP or OCBOA *not* called for by the prescribed form

2. Departures from requirements of the prescribed form

GAAP (OCBOA) Departures Not Called for by the Prescribed Form

10.302 If the accountant becomes aware of a material departure from GAAP or OCBOA that is not required by the prescribed form, the form must either be revised or the departure must be disclosed in the accountant's compilation report. The report is modified by adding a separate paragraph describing the departure and the effects of the departure if they are known. If the effects are not known, the separate paragraph must include a statement that the effects of the departure have not been determined. (See section 10.706 for an illustrative report.)

10.303 SSARS No. 3 recognizes two ways in which a prescribed form can require a GAAP or OCBOA departure. First, the form or related instructions may specify a measurement principle that differs from GAAP or OCBOA. For example, the prescribed form may require that property, plant, and equipment be presented at market value rather than at depreciated cost. The important factor for the accountant to consider is that the form (or related instructions) must specifically require a measurement principle that differs from GAAP or OCBOA. If the form or instructions are silent about the measurement principle to be used, then GAAP or OCBOA should be followed.

10.304 The second way in which a prescribed form can require a GAAP or OCBOA departure pertains to disclosures. Under SSARS No. 3, if the prescribed form or related instructions do not require a specific disclosure, then omission of the disclosure is required by the prescribed form. That is, when the prescribed form is silent about a disclosure, the accountant may presume that the disclosure is not called for by the prescribed form.

10.305 Sometimes, the prescribed form may not specify the basis of accounting to be used in compiling the financial statements included in the form. That is, the form may not specifically state that GAAP or OCBOA (cash or tax basis) should be used. In such circumstances, the basis of accounting the client uses to prepare its financial statements should be used for the prescribed form. The accountant can then compare the requirements in the prescribed form with that basis to determine what departures are called for by the prescribed form. For example, if the prescribed form does not specify a basis of accounting and the client uses the cash basis to prepare its financial statements, then the cash basis of accounting becomes the reference point for determining departures from OCBOA called for by the prescribed form. (See sections 10.704 and 10.705 for illustrative reports on OCBOA financial statements in prescribed forms.)

Departures from Requirements of the Prescribed Form

10.306 If the accountant becomes aware of a material departure from a requirement of the prescribed form, the form must either be revised or the departure must be disclosed in the accountant's compilation report. The report is modified by adding a separate paragraph describing the departure and the effects of the departure if they are known. If the effects are not known, the separate paragraph must include a statement that the effects of the departure have not been determined.

10.307 This type of departure can occur when the client is unable to provide specific information required by the form. For example, a prescribed form may require that land be stated at appraisal value but the client may not have determined that value and, instead, reports the land at cost. In this circumstance, the accountant's compilation report should disclose the departure from the requirements of the prescribed form. Note that the departure should be disclosed even though land is reported using a GAAP measurement principle (cost), because the form calls for a different measurement principle. (See section 10.707 for an illustrative report.)

10.400 COMPILING PRESCRIBED-FORM FINANCIAL STATEMENTS FROM PREVIOUSLY REVIEWED OR AUDITED FINANCIAL STATEMENTS

10.401 In some circumstances, an accountant may be asked to compile financial statements in a prescribed form that calls for GAAP or OCBOA departures from financial statements that he or she previously reviewed or audited. The authors believe that such a service is permissible under SSARS. Footnote No. 2 of SSARS No. 3 specifically recognizes that compiling financial statements in a prescribed form from financial statements the accountant has previously reviewed is acceptable. Based on this footnote, compilation of prescribed-form statements from statements that were previously audited should also be presumed to be appropriate.

10.402 When the accountant compiles prescribed form statements from statements previously reviewed or audited, the question arises as to whether the accountant's SSARS No. 3 compilation report should refer to the report on the previous service. There is no requirement for the accountant to refer to a previous service. Thus, the accountant may issue the standard SSARS No. 3 report in these circumstances.

10.403 However, SSARS No. 3, Interpretation No. 1, *Omission of Disclosures in Financial Statements Included in Certain Prescribed Forms*, allows the accountant to refer to a previous review service in a prescribed form report as long as the measurement principles used in the compiled statements do not cause them to be materially different from the reviewed statements. That is, when differences in the two sets of financial statements is limited to the omission of disclosures not requested by the prescribed form (as opposed to measurement differences), reference to the prior review report is permitted. Based on the rationale underlying this interpretation, referral to a prior audit report should also be considered appropriate under similar circumstances.

10.404 When the accountant refers to a previously-issued report, the guidance in Interpretation No. 1 should be followed in preparing the report on the prescribed form financial statements. The Interpretation suggests that the following paragraph be added to the SSARS No. 3 report when a review was previously performed:

> These financial statements were compiled by me (us) from financial statements for the same period which I (we) previously reviewed, as indicated in my (our) report dated
>
> ________.

This paragraph can also be adapted for a prior audit service. (See sections 10.708 and 10.709 for illustrative reports.)

10.405 The Interpretation also states that the reference to a previous review report should include a description or quotation of any modifications of the standard review report previously issued and of any paragraphs emphasizing a matter regarding the financial statements.

10.500 SUPPLEMENTARY INFORMATION ACCOMPANYING PRESCRIBED FORMS

10.501 When supplementary information accompanies financial statements included in a prescribed form, the accountant must indicate the responsibility, if any, he or she assumes for that information. That is, the accountant must follow the reporting requirements set forth in SSARS No. 1 for such information. (The definition of supplementary information and the related reporting requirements are discussed in detail in sections 5.131 and 5.132 of Chapter 5.)

10.502 The accountant's SSARS No. 3 report should be modified to address the supplementary information in a manner similar to that illustrated in SSARS No. 1. If the accountant has compiled the information, the report should be modified to indicate that fact. (See section 10.710 for an illustrative report.)

10.503 If the accountant has not compiled, reviewed, or audited the supplementary information and, therefore, assumes no responsibility for it, he or she should modify the SSARS No. 3 report accordingly. (See section 10.711 for an illustrative report.)

10.600 RMA BUSINESS CREDIT INFORMATION PACKAGE (BCIP)

10.601 In 1993, Robert Morris Associates (RMA), an association of bank loan and credit officers, published its Business Credit Information Package (BCIP). The BCIP is designed to provide bankers with useful financial information at a reasonable cost to the prospective borrower. To accomplish this objective, the BCIP includes, among other items, a prescribed form for financial statements. Bankers can adopt this prescribed form for any or all of their loan applicants and thus allow their accountants to use the special provisions of SSARS No. 3. The authors' observation is that the BCIP is not being widely used; however, an accountant may find him/herself asked to report on one.

Practice Tip:

A bank does not need to adopt the BCIP prescribed-form financial statements for all of its borrowers to meet the requirements of SSARS No. 3 concerning prescribed forms. A bank may adopt the form for some borrowers and establish other requirements (such as full GAAP financial statements) for other borrowers. For those borrowers for whom the bank adopts the BCIP form, the accountant may use the reporting option provided by SSARS No. 3. In any event, before using the BCIP prescribed form, be sure that the Bank has adopted that form for your client.

10.602 The BCIP prescribed-form financial statements consist of the following for the current year and prior year:

- Balance Sheet
- Statement of Operations
- Statement of Changes in Equity
- Statement of Cash Flows
- Reconciliation of Net Income to Net Cash Provided (Used) by Operating Activities

10.603 The prescribed form requires the *amounts* in these financial statements to be presented in accordance with GAAP recognition and measurement standards. That is, there are no differences between the requirements of the form and GAAP for determining the amounts of assets, liabilities, revenues, expenses, etc. in the financial statements. The form, however, does not require all of the *disclosures* that GAAP requires. Instead, it prescribes that only 11 specific disclosures be included in the financial statements. These 11 disclosures, however, must be presented in accordance with GAAP requirements.

10.604 The prescribed-form financial statements contain the typical sections and line items commonly included in GAAP financial statements. In addition, each section of the form contains several blank lines for other line items that may pertain to a particular category. For example, the current assets section includes typical current asset accounts plus blank lines for other current assets a particular borrower might have. Thus, the form requires that the financial statements include all material items that pertain to a particular financial statement section.

Supplementary Information in BCIP

10.605 The prescribed-form financial statements section of the BCIP also contains two supplementary schedules that a banker may request — a schedule of cost of sales and a schedule of operating expenses. When the banker asks the client to provide supplementary information, the BCIP requires that the accountant compile that information. Therefore, the supplementary information should be addressed in the accountant's report.

Other Elements of the BCIP

10.606 In addition to the prescribed-form financial statements (including the 11 disclosures), the BCIP includes four other elements:

- A request letter (banker prepared) that specifies the banker's information needs and documents the banker's adoption of the BCIP prescribed-form financial statements. A copy of this letter normally would be obtained from the client.
- A borrower questionnaire (borrower and/or accountant prepared) that provides general information about the borrower's business, such as major products, services, and operations; significant changes; customers and suppliers; and accounting policies and procedures.
- A reporting and disclosures checklist (accountant prepared) to assist the accountant in compiling the prescribed financial statements and any supplementary information that may be specified. This checklist (see section 10.800) would be used in lieu of the checklist presented in section 14.600 of this Manual.
- An illustrative accountant's report using the SSARS No. 3 alternative (see sections 10.607 and 10.608).

Practice Tip:

The reporting and disclosure checklist is intended solely for the accountant's use and should be retained in the accountant's compilation workpapers, not given to the banker. The form is intended to remind the accountant of matters to be considered.

Accountant's Report

10.607 When the banker adopts the prescribed-form financial statements contained in the BCIP, the accountant may issue a compilation report in accordance with the SSARS No. 3 alternative. Specifically, the departures from GAAP disclosure requirements called for by the form need not be identified in the accountant's compilation report. The accountant should remember, however, that material departures from GAAP recognition and measurement requirements would have to be identified in the accountant's report as would any material departures pertaining to the 11 disclosures prescribed by the BCIP.

10.608 Although the BCIP contains an illustrative SSARS No. 3 report, the authors recommend that accountants use the report form illustrated in 10.712 instead of the BCIP illustration. The BCIP report illustration identifies the supplementary information in the first paragraph, but fails to refer to the supplementary information in the second and third paragraphs. The authors believe that the report illustrated in 10.712 more clearly communicates the accountant's responsibility by referring to the supplementary information in the second and third paragraphs.

10.609 Although the BCIP was published in booklet form, software formats are likely to be developed. If software format financial statements adhere to the prescribed-form financial statement requirements in the BCIP, the authors believe they meet the definition of a prescribed form in SSARS No. 3. In such cases, the accountant may report on the software version of the BCIP financial statements using the SSARS No. 3 alternative. The report may be included in the computer media (disk or modem communication) or may be in hard copy form and accompany the computer media.

10.610 The Business Credit Information Package is reprinted in its entirety in section 10.800.

Practice Tip:

To qualify for use of the optional report under SSARS No. 3, the accountant should present the financial statements on the prescribed form included in the Business Credit Information Package or a computer template that is virtually identical.

10.700 SAMPLE REPORTS

10.701 The following pages include illustrative reports for various engagements involving prescribed forms.

10.702 The illustrative reports are included on the Wordperfect diskette provided with the manual.

Sample Reports on Prescribed Forms

10.703 Standard Prescribed-Form Compilation Report

____
____
____

I (We) have compiled the __________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

My (Our) compilation was limited to presenting in the form prescribed by _______________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them.

These financial statements (including the related disclosures) are presented in accordance with the requirements of _______________ [name of the body], which differ from generally accepted accounting principles. Accordingly, these financial statements are not designed for those who are not informed about such differences.

[Signature]

[Date]

10.704 Prescribed-Form Compilation Report, Financial Statements on the Modified Cash Basis

____
____
____

I (We) have compiled the ______________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. The financial statements have been prepared on the modified cash basis of accounting in accordance with the prescribed form, which is a basis of accounting other than generally accepted accounting principles.

My (Our) compilation was limited to presenting in the form prescribed by ________________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them.

These financial statements (including the related disclosures) are presented in accordance with the requirements of __________________ [name of the body], which differ from the modified cash basis of accounting. Accordingly, these financial statements are not designed for those who are not informed about such differences.

[Signature]

[Date]

10.705 Prescribed-Form Compilation Report, Financial Statements on the Income Tax Basis

____
____
____

I (We) have compiled the ______________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. The financial statements have been prepared on the income tax basis of accounting in accordance with the prescribed form, which is a basis of accounting other than generally accepted accounting principles.

My (Our) compilation was limited to presenting in the form prescribed by ________________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them.

These financial statements (including the related disclosures) are presented in accordance with the requirements of _________________ [name of the body], which differ from the income tax basis of accounting. Accordingly, these financial statements are not designed for those who are not informed about such differences.

[Signature]

[Date]

10.706 Prescribed-Form Compilation Report, GAAP Departures Not Required by Form and Effects Have Not Been Determined

____
____
____

I (We) have compiled the ____________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

My (Our) compilation was limited to presenting in the form prescribed by __________________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them. However, I (we) did become aware of a departure from generally accepted accounting principles that is not called for by the prescribed form or related instructions, as described in the following paragraph.

Generally accepted accounting principles require that inventory cost consist of material, labor, and overhead. Management has (The owners have) informed me (us) that the inventory of finished goods and work in process is stated in the accompanying financial statements at material and labor cost only, and that the effect of this departure from generally accepted accounting principles has not been determined.

These financial statements (including the related disclosures) are presented in accordance with the requirements of ________________ [name of the body], which differ from generally accepted accounting principles. Accordingly, these financial statements are not designed for those who are not informed about such differences.

[Signature]

[Date]

10.707 Prescribed-Form Compilation Report, Departures from Requirements of the Form and Effects Have Not Been Determined

____

____

____

I (We) have compiled the ___________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

My (Our) compilation was limited to presenting in the form prescribed by ________________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them. However, I (we) did become aware of a departure from the requirements of the prescribed form, as described in the following paragraph.

The prescribed form requires that land be stated at its appraised value. Management has (The owners have) informed me (us) that land is stated in the accompanying financial statements at cost less depreciation. The effect of this departure from the requirements of the prescribed form has not been determined.

These financial statements (including the related disclosures) are presented in accordance with the requirements of ________________ [name of the body], which differ from generally accepted accounting principles. Accordingly, these financial statements are not designed for those who are not informed about such differences.

[Signature]

[Date]

10.708 Prescribed-Form Compilation Report, Financial Statements Previously Reviewed

____
____
____

I (We) have compiled the __________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

My (Our) compilation was limited to presenting in the form prescribed by ______________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them. These financial statements were compiled by me (us) from financial statements for the same period which I (we) previously reviewed, as indicated in my (our) report dated _________.[1]

These financial statements (including the related disclosures) are presented in accordance with the requirements of _______________ [name of the body], which differ from generally accepted accounting principles. Accordingly, these financial statements are not designed for those who are not informed about such differences.

[Signature]

[Date]

Note:

[1] The reference to the previously reviewed financial statements is appropriate only if the measurement principles used in the two sets of financial statements are not materially different. (See section 10.403.)

10.709 Prescribed-Form Compilation Report, Financial Statements Previously Audited

____
____
____

I (We) have compiled the __________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

My (Our) compilation was limited to presenting in the form prescribed by _______________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them. These financial statements were compiled by me (us) from financial statements for the same period which I (we) previously audited, as indicated in my (our) report dated _________.[1]

These financial statements (including the related disclosures) are presented in accordance with the requirements of _______________ [name of the body], which differ from generally accepted accounting principles. Accordingly, these financial statements are not designed for those who are not informed about such differences.

[Signature]

[Date]

Note:

[1] The reference to the previously reviewed financial statements is appropriate only if the measurement principles used in the two sets of financial statements are not materially different. (See section 10.403.)

10.710 Prescribed-Form Compilation Report, Accompanying Supplementary Information Has Been Compiled

____

____

____

I (We) have compiled the __________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. I (We) have also compiled the supplementary information presented in the prescribed form.

My (Our) compilation was limited to presenting in the form prescribed by ______________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements or supplementary information referred to above and, accordingly, do not express an opinion or any other form of assurance on them.

These financial statements (including the related disclosures) and supplementary information are presented in accordance with the requirements of _____________ [name of the body], which differ from generally accepted accounting principles. Accordingly, these financial statements and supplementary information are not designed for those who are not informed about such differences.

[Signature]

[Date]

10.711 Prescribed-Form Compilation Report, Accompanying Supplementary Information Has Not Been Compiled

____

____

____

I (We) have compiled the ______________________________ [identify financial statements, including periods presented and name of client] included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

My (Our) compilation was limited to presenting in the form prescribed by ________________ [name of the body] information that is the representation of management (the owners). I (We) have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them.

These financial statements (including the related disclosures) are presented in accordance with the requirements of ________________ [name of the body], which differ from generally accepted accounting principles. Accordingly, these financial statements are not designed for those who are not informed about such differences.

The supplementary information contained in the accompanying prescribed form has not been audited, reviewed, or compiled by me (us) and, accordingly, I (we) assume no responsibility for that information.

[Signature]

[Date]

10.712 Prescribed-Form Compilation Report For BCIP, Accompanying Supplementary Information Has Been Compiled

____
____
____

I (We) have compiled the ____________________________ [identify financial statements, including periods presented and name of client] included in the accompanying Business Credit Information Package in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. I (We) have also compiled the supplementary information presented in the Business Credit Information Package.

My (Our) compilation was limited to presenting in the form designed by Robert Morris Associates (the "Business Credit Information Package") and requested by _______________ [name of bank] information that is the representation of management. I (We) have not audited or reviewed the financial statements or supplementary information referred to above and, accordingly, do not express an opinion or any other form of assurance on them.

These financial statements (including the related disclosures) and supplementary information are for the use of _______________ [name of bank] and are presented in accordance with the requirements of the Business Credit Information Package, which differ from generally accepted accounting principles. Accordingly, these financial statements and supplementary information are not designed for those who are not informed about such differences.

[Signature]

[Date]

10.800

rma
ROBERT MORRIS ASSOCIATES

Business Credit Information Package

Bankers prefer borrowers' financial statements accompanied by independent accountants' reports conveying the highest possible level of assurance. This Business Credit Information Package has been developed for use by borrowers when, by mutual agreement between borrower and banker, compilation services by an independent accountant will be utilized.

About Robert Morris Associates

Robert Morris Associates (RMA) is the association of bank loan and credit officers. Founded in 1914, RMA has grown to almost 3,000 commercial banks and thrift institutions, which account for nearly 80% of the C&I lending done by U.S. commercial banks. These institutions are represented in the association by almost 15,000 commercial loan and credit officers and related personnel in all 50 states, Puerto Rico, Canada, and several offshore cities.

RMA was named after the American patriot who signed the Declaration of Independence, was largely responsible for the financing of our Revolutionary War, and helped establish our banking system.

The association's original purpose back in 1914 was to facilitate the flow and interchange of credit information. Today, this purpose has been expanded to include working continuously to improve the principles and practices of commercial lending, loan management, credit administration, and related areas in its member institutions and others in the financial services industry.

RMA seeks to fulfill its purpose by providing commercial bankers with programs, products, and services they need to increase their proficiency in lending, credit, and related areas. RMA's reason for being, then, is to provide these bankers with the tools they need to make better loans, keep abreast of the continual changes that affect the lending function, and, at the bottom line, help them increase the profitability of their institutions.

While Robert Morris Associates believes the material contained in this publication is accurate, the conclusions and opinions expressed are those of the authors. Moreover, no opinion expressed on a legal matter should be relied on without the advice of counsel familiar with both the facts in a particular case and the applicable law.

Additional copies of this publication are available from the Customer Service Department, Robert Morris Associates, One Liberty Place, Suite 2300, Philadelphia, PA 19103-7398 (215) 851-0585.

FOREWORD

The following commentary was written by Michael W. Sperry, executive vice president, Southern National Corporation, and member of the Robert Morris Associates Accounting Policy Committee (APC). Mr. Sperry served as chairman of the APC Task Force that produced this document. The task force gratefully acknowledges the significant contributions of the Technical Issues Committee of the Private Company Practice Section of the American Institute of Certified Public Accountants (AICPA).

In spring 1993, the Accounting Policy Committee of Robert Morris Associates (RMA) convened a task force to study means by which financial information from privately owned businesses could be developed without significant cost to the provider. This **Business Credit Information Package** (BCIP) is the product of this effort.

Here is how it works. The banker issues a **Request Letter** to the business borrower, agreeing in writing to accept financial statements prepared in the BCIP format, on condition that the borrower complete an **RMA Business Borrower Questionnaire** and provide other relevant information. Based on this letter, the financial statements are prepared in accordance with the **Reporting and Disclosure Checklist and Prescribed Form for the Preparation of Financial Statements**, and the accountant issues an **Accountant's Report** in the form illustrated in the BCIP. The five elements of the BCIP are as follows:

<u>Request Letter</u>. This letter serves two purposes. It functions as a checklist for the banker to communicate information needs and documents the banker's willingness to accept (in connection with a specific loan request) financial statements in the BCIP format. Commonly requested types of supplemental financial information are itemized on the checklist, and blanks are provided for requesting types of information not otherwise listed.

<u>RMA Business Borrower Questionnaire</u>. This form contains questions about a firm's accounting system and other pertinent facts bankers generally need in a lending situation. It was designed as a supplement to financial statements that are prepared in the BCIP format. Bankers may, of course, request whatever information they desire; this questionnaire is a convenient form for transmitting questions and obtaining answers on accounting and financial issues.

<u>Reporting and Disclosure Checklist</u>. This is a checklist for accountants to use when preparing financial statements in the BCIP format. It lists the various types of financial statements that must be included, the degree of detail required for each, and the footnotes that must accompany the statements. Although this form is a tool for the accountant's use, it gives bankers an overview of what they will receive when financial statements are prepared in the BCIP format.

<u>Prescribed Form for the Preparation of Financial Statements</u>. This form is designed to present two-year comparative figures for the balance sheet, income statement, statement of changes in equity, and statement of cash flows. Eleven footnotes also are required. The statements will not contain all footnotes that are required in a full generally accepted accounting principles (GAAP) presentation, but enough are included to answer most of the questions that arise in the credit analysis process.

Accountant's Report. A specific format is recommended for the accountant's report that accompanies financial statements presented in the BCIP. The report cites the BCIP as the format for the presentation and identifies the bank that has agreed to accept statements in this format. It provides that the financial statements, presented in the BCIP format, were compiled in accordance with the AICPA's Statements on Standards for Accounting and Review Services (SSARS No. 3, "Compilation Reports on Financial Statements Included in Certain Prescribed Forms").

In essence, the RMA Business Credit Information Package is a compromise. Like most compromises, it is not a cure-all. It is not a viable approach when circumstances dictate the need for full GAAP disclosures. However, it offers a reasonable alternative to compilations with no footnotes and is a cost-effective alternative for those situations in which all parties involved can agree to its use. It provides bankers with comprehensive sets of financial statements, presented in a defined format, together with specific disclosures. It is a tool for managing information risk that bankers can employ to their benefit. It may allow accountants to reduce fees for such services. And it enables business owners to satisfy their bankers' information needs without incurring significant costs. In situations where it can be used, everybody wins.

Policy Division
Robert Morris Associates
Philadelphia, Pennsylvania

HOW TO USE THIS PACKAGE:

Banker:
Reproduce the Request Letter (page 3 of this package) on bank letterhead, indicating the required information. Review Request Letter and this package with (prospective) borrower.

Borrower:
Complete Business Borrower Questionnaire (pages 4-7) and return to banker. Give the Reporting and Disclosure Checklist, Prescribed Form for the Preparation of Financial Statements, and Sample Accountant's Report to your independent accountant (pages 8-19) along with a copy of the Request Letter. (Note: Either the borrower or the accountant may prepare the financial statements.) Upon receipt from accountant, return statements with disclosures and accountant's report to your banker.

Accountant:
Upon receipt from client (borrower), review requirements of Request Letter, Reporting and Disclosure Checklist, Prescribed Form for the Preparation of Financial Statements, and Sample Accountant's Report. Then, complete the engagement, reproduce and sign the Accountant's Report (page 19 of this package) and forward all materials to client.

Robert Morris Associates
Business Credit Information Package

Request Letter

[Bank Letterhead]

[Date]

[Prospective Borrower's Name]
[Mailing Address]

Dear _______

In order to facilitate consideration of the credit request you have made of our bank, we request that you provide information concerning your company as follows:

FINANCIAL STATEMENTS FOR THE FISCAL YEARS [Specify YEARS]:
[Check One]

- ☐ Compiled by CPA firm — full GAAP presentation.
- ☐ Compiled by CPA firm — **Business Credit Information Package** presentation.

SUPPLEMENTAL INFORMATION (Provide all information checked):
[Check boxes as appropriate]

- ☐ Interim financial statements (if ____ months have passed since the last fiscal year-end, provide all available interim statements).
- ☐ RMA Business Borrower Questionnaire (completed by the prospective borrower) (pages 4–7).
- ☐ Copies of company's income tax returns for the past three years.
- ☐ Copies of owner's income tax returns for the past three years.
- ☐ Owner's current personal financial statement.
- ☐ Copies of loan agreements for all existing credit facilities.
- ☐ Copy of current actuarial report for defined benefit plans.
- ☐ ____
- ☐ ____

Sincerely,
[Bank Officer's Name and Title]

Attachments— —List as appropriate
Business Borrower Questionnaire
Reporting and Disclosure Checklist
Prescribed Form for the Preparation of Financial Statements
Sample Accountant's Report

Robert Morris Associates
Business Credit Information Package
Business Borrower Questionnaire

Attach additional sheets if needed to complete any section

Borrower Name (exact legal title):		
Address:		Tax ID Number:
Prepared By:	Date	Phone Number:

Accountant:	Phone Number:
Attorney:	Phone Number:
Insurance Agent:	Phone Number:

Describe the company's major products or services, markets, and methods of operation.

Describe any significant changes in earnings and financial condition over the past three years and the reasons they occurred.

Describe significant changes expected in the coming year (e.g., asset purchases, new revenue sources, expense increases).

List the company's five largest customers, credit terms offered to each, and the percentage of annual sales to each.

Customer's Name and Address	Credit Terms	% of Sales
1		
2		
3		
4		
5		

List the company's five largest suppliers, credit terms from each, and credit limits from each.

Supplier's Name and Address	Credit Terms	Credit Limit
1		
2		
3		
4		
5		

Are any examinations by taxing authorities for sales, income, excise, or other taxes now in process?

☐ Yes ☐ No If yes, describe: Date of last IRS Audit: ____________

Are any tax payments (sales, income, payroll, property, etc.) delinquent?

☐ Yes ☐ No If yes, describe:

Is the company currently involved in any lawsuits or pending litigation?

☐ Yes ☐ No If yes, describe:

Does the company have an ownership succession plan (e.g., buy-sell agreement)?

☐ Yes ☐ No If yes, describe:

INSURANCE COVERAGE	DOLLAR AMOUNT	INSURANCE COMPANY NAME
Inventories		
Fixed Assets		
General Liability		
Business Interruption		
Product Liability		
Key Person Life		
Other:		

List owners/partners/shareholders, the percentage of the company they own, and their compensation from the company for the past two years. Include all amounts paid by the company (salary, bonus, interest, dividends, other amounts on Forms W2 and 1099).

Name	Position/Title	% Owned	Total Compensation	
			19	19

Are there any amounts due to the company from owners or other related parties?

☐ Yes ☐ No If yes, describe:

Is your company in compliance with applicable federal and state regulations (such as environmental, employment, or safety)?

☐ Yes ☐ No If no, describe:

Has your company ever been cited for a violation of any of these regulations?

☐ Yes ☐ No If yes, describe:

SAMPLE

ACCOUNTING POLICIES & PROCEDURES	Yes	No	N/A	Comments
Cash Account Are all bank accounts reconciled monthly?				
Accounts Receivable Are agings prepared monthly?				
Are agings reviewed monthly for possible bad debts? If not monthly, how often?________________				
Are all credit memos approved in writing?				
Are credit memos issued by someone other than the person who posts cash receipts?				
Are unusual sales terms offered (dated billings, bill-and-hold, consignment)?				
Inventory Are perpetual inventory records maintained?				
Are physical inventories taken monthly? If not monthly, how often?________________				
Are inventory turnover rates (cost of sales divided by inventory) calculated for each product type and reviewed at least quarterly?				
Are signed shipping receipts obtained and maintained?				
Accounts Payable Are agings prepared monthly?				
Are payables posted by someone other than the the person who disburses funds?				
Taxes Is an outside payroll preparation service used?				
Are accrued payroll taxes set aside at the time payroll checks are issued?				
Are any tax returns (payroll, sales, income, etc.) delinquent?				
Are income tax estimates filed and paid quarterly? If not quarterly, how often?________________				
Leases Are assets leased from owners evidenced by written agreements?				
Loans from Owners Are debts to owners evidenced by signed notes?				
Are debts to owners formally subordinated to other creditors?				
Financial Statements Are financial statements prepared internally on a monthly basis?				
Are cash, accounts receivable, inventory, and accounts payable reconciled to the general ledger on a monthly basis?				

SAMPLE

BORROWER'S CERTIFICATION: The responses given in this questionnaire are true, accurate, and complete to the best of my knowledge. Company:______________________________ By:______________________________ Date:________	This questionnaire is designed to provide the minimum financial information necessary to bankers in making commercial lending decisions when the prospective borrower's financial statements are compiled, but do not contain full GAAP disclosures. Bankers may require additional information and will consider other factors that are not part of this questionnaire. The bank's receipt of this completed questionnaire does not guarantee that a loan request will be approved.

Robert Morris Associates

Business Credit Information Package

Reporting and Disclosure Checklist

Solely for Accountant's Workpapers

Full GAAP compilations (i.e., financial statements with all required note disclosures) are always preferable. If the client's banker permits the RMA Business Credit Information Package selected disclosure alternative, the Prescribed Form requires the amounts in the financial statements be presented in accordance with GAAP rules for recognition and measurement but permits omission of certain disclosures except those identified in this Reporting and Disclosure Checklist. Any material GAAP measurement departures or departures from the 11 disclosures require that the accountant's report be modified, as required by Statement on Standards for Accounting and Review Services No. 3, "Compilation Reports on Financial Statements Included in Certain Prescribed Forms" (SSARS No. 3.)

	Check off as considered
FINANCIAL STATEMENTS	
1. GAAP is the basis to be used for recognition and measurement purposes.	______
2. Two year comparative statements (not applicable retroactively) for fiscal year-end statements:	
a. Balance sheet	______
b. Income statement	______
c. Statement of changes in owners equity	______
d. Statement of cash flows*	______
3. If the income statement is condensed, supplementary schedules are included for:	
a. Cost of goods sold	______
b. Operating expenses	______
4. Each page in the financial statements includes a reference to the accountant's compilation report.	______
ACCOUNTANT'S REPORT	
1. Compilation report in compliance with SSARS No. 3.	______
2. Supplementary information is provided.	______
3. Any material departures from GAAP recognition and measurement or disclosures required by the BCIP are disclosed (See paragraph 4, SSARS No. 3).	______
4. Report is dated and signed.	______

SAMPLE

*RMA recognizes that both the direct and indirect method are permitted by GAAP; however, as explained in RMA's publication titled *Financial Statements for Bank Credit Purposes,* the direct method provides superior and uniquely valuable information for the bank lender's purposes. Consequently, and especially in situations where lenders do not have full GAAP disclosures, the direct method presentation is preferred.

Check off as considered

REQUIRED DISCLOSURES (Footnotes)

1. Organization and nature of business ______
2. Summary of significant accounting policies:
   a. Basis of accounting ______
   b. Revenue recognition method ______
   c. Inventory composition, basis of valuation, and cost determination method ______
   d. Depreciation methods and estimated useful lives of depreciable assets ______
   e. Method used to account for income taxes ______
3. Allowance for bad debts ______
4. Marketable equity securities—aggregate cost and market values with identification of which is carrying value ______
5. Debt
   a. Repayment terms, interest rates, maturity dates, and collateral ______
   b. Lines of credit—committed amounts, maturity dates, and unused availability ______
   c. Minimum annual maturities for the next five years ______
6. Leases
   a. General description of leasing arrangements ______
   b. Future minimum rental payments required as of the date of the latest balance sheet in aggregate and for each of the five succeeding fiscal years ______
7. Related party transactions
   a. Description of the transaction and nature of the relationship ______
   b. Dollar amount of transactions ______
   c. Amounts due to or from related parties ______
8. Pension plans
   a. Description of the plans including employee groups covered ______
   b. Pension expense for period presented and how calculated ______
   c. Unfunded pension liability ______
9. Income tax expense ______
10. Interest and income taxes paid—either as a footnote or on the face of the statement of cash flows ______
11. Significant subsequent events ______

Business Credit Information Package – Prescribed Form

Borrower's Name ____________________

Balance Sheet Date

Assets	________	________
Current Assets	XXXXX	XXXXX
Cash and cash equivalents		
Short–term investments		
Accounts receivable		
Allowance for doubtful accounts	( )	( )
Notes receivable		
Inventories		
Prepaid expenses		
____________________		
____________________		
____________________		
Total Current Assets		
Property and Equipment	XXXXX	XXXXX
Land		
Buildings		
Machinery and equipment		
Trucks and automobiles		
Office furniture and equipment		
Assets under capital lease		
____________________		
____________________		
Total Property and Equipment		
Less accumulated depreciation and amortization	( )	( )
Net Property and Equipment		
Other Assets	XXXXX	XXXXX
Cash surrender value of officer's life insurance		
Loans against policies	( )	( )
Notes receivable		
Organization costs (net)		
____________________		
____________________		
____________________		
Total Other Assets		
Total Assets		

See Accountant's Report

SAMPLE

Business Credit Information Package – Prescribed Form

Borrower's Name ____________________

Balance Sheet

Liabilities and Equity

	Date	
	________	________
Current Liabilities	XXXXX	XXXXX
Lines of credit		
Notes payable – current portion		
Accounts payable		
Accrued and withheld payroll taxes		
Accrued expenses		
____________________		
____________________		
____________________		
Total Current Liabilities		
Long–Term Liabilities	XXXXX	XXXXX
Notes payable		
____________________		
____________________		
____________________		
Total Long–Term Liabilities		
Total Liabilities		
Equity	XXXXX	XXXXX
Common stock		
Additional paid–in capital		
Less treasury stock	( )	( )
Retained earnings		
Partners' capital		
Owners' equity		
____________________		
____________________		
Total Equity		
Total Liabilities and Equity		

See Accountant's Report

Business Credit Information Package – Prescribed Form

Borrower's Name ____________________

Statement of Operations

Date

	________	________
Income	XXXXX	XXXXX
Sales (net)		
Fees		
________________		
________________		
________________		
Total Income		
Cost of Sales		
Gross Profit		
Operating Expenses	XXXXX	XXXXX
________________		
________________		
________________		
Total Operating Expenses		
Income from Operations		
Other Income (Expense)	XXXXX	XXXXX
________________		
________________		
________________		
________________		
Total Other Income (Expense)		
Income before Taxes		
Provision for Income Taxes		
Income before Extraordinary Items		
Extraordinary Items	XXXXX	XXXXX
________________		
________________		
Total Extraordinary Items		
Net Income		

See Accountant's Report

Business Credit Information Package – Prescribed Form

Borrower's Name ____________________

Statement of Changes in Equity

	Common Stock # Shares	Common Stock Amount	Additional Paid–In Capital	Treasury Stock	Retained Earnings/ Owners'/ Partners' Equity	Total
Beginning Balance ____________ (Date)						
Stock Issued/ Capital Contributions						
Stock Retired						
Net Income						
Dividends/Distributions/ Withdrawals						
Balance ____________ (Date)						
Stock Issued/Capital Contributed						
Stock Retired						
Net Income						
Dividends/Distributions/ Withdrawals						
Balance ____________ (Date)						

See Accountant's Report

Business Credit Information Package – Prescribed Form

Borrower's Name ____________

Statement of Cash Flows

	Date	
	________	________
Cash Flows from Operating Activities:	XXXXX	XXXXX
Cash received from customers		
Cash paid to suppliers and employees		
Interest received		
Interest paid		
Income taxes paid		
____________		
____________		
____________		
Net Cash Provided (Used) by Operating Activities		
Cash Flows from Investing Activities:	XXXXX	XXXXX
Proceeds from sale of assets		
Purchases of property and equipment		
____________		
____________		
____________		
Net Cash Provided (Used) by Investing Activities		
Cash Flows from Financing Activities:	XXXXX	XXXXX
Net borrowings under line of credit agreement		
Proceeds from new borrowings		
Repayment of loans		
Principal payments under capital lease obligations		
Dividends/distributions/withdrawals paid		
Proceeds from issuance of stock		
Partner/owner capital contributions		
____________		
____________		
____________		
Net Cash Provided (Used) by Financing Activities		
Net Increase (Decrease) in Cash and Cash Equivalents		
Cash and Cash Equivalents, Beginning		
Cash and Cash Equivalents, Ending		
Schedule of Noncash Investing and Financing	XXXXX	XXXXX
Transactions: ____________		
____________		
____________		

See Accountant's Report

Business Credit Information Package – Prescribed Form

Borrower's Name ____________

Reconciliation of Net Income to Net Cash Provided (Used) by Operating Activities

	Year	Year
Net Income		
Adjustments to reconcile net income to net cash provided by operating activities:	XXXXX	XXXXX
Depreciation and amortization		
____________		
____________		
____________		
(Increase) decrease in assets and increase (decrease) in liabilities:	XXXXX	XXXXX
Accounts receivable		
Inventories		
Prepaid expenses		
Accounts payable		
Accrued and withheld payroll taxes		
Accrued expenses		
____________		
____________		
____________		
____________		
Net Cash Provided (Used) by Operating Activities		

See Accountant's Report

Business Credit Information Package – Prescribed Form

Borrower's Name ____________________

Required Disclosures

Note: See Reporting and Disclosure Checklist for required disclosures

Business Credit Information Package – Prescribed Form

Borrower's Name ____________________
Supplementary Schedule of Cost of Sales

For the Years Ended

	Date	Date
Beginning Inventory		
Purchases		
Salaries		
Overhead		
____________________		
____________________		
____________________		
____________________		
Ending Inventory		
Cost of Sales		

See Accountant's Report

Business Credit Information Package – Prescribed Form

Borrower's Name ______________________

Supplementary Schedule of Operating Expenses

For the Years Ended ____________ ____________

	Date	Date
Salaries and Wages		
Payroll Taxes		
Employee Benefits		
Total Personnel Costs		
Other Expenses		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
____________________		
Total Operating Expenses		

SAMPLE

See Accountant's Report

Robert Morris Associates
Business Credit Information Package

Sample Accountant's Report for Financial Statements Prepared in Accordance with RMA's Business Credit Information Package

[To the Board of Directors]
[XYZ Company]
[City, State]

We have compiled the [identification of financial statements and supplementary schedules, including period covered and name of entity] included in the accompanying Business Credit Information Package in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

Our compilation was limited to presenting in the form designed by Robert Morris Associates (the "Business Credit Information Package") and requested by [name of bank] information that is the representation of management. We have not audited or reviewed the financial statements referred to above and, accordingly, do not express an opinion or any other form of assurance on them.

These financial statements (including related disclosures) are for the use of [name of bank] and are presented in accordance with the requirements of the Business Credit Information Package, which differ from generally accepted accounting principles. Accordingly, these financial statements are not designed for those who are not informed about such differences.

[Firm's signature]
[Date]

ROBERT MORRIS ASSOCIATES
The Association of Bank Loan and Credit Officers
One Liberty Place, Suite 2300, Philadelphia, PA 19103-7398

31201 10M 9/93

Personal
Financial Statements

CHAPTER 11

PERSONAL FINANCIAL STATEMENTS

Table of Contents

CHAPTER 11

PERSONAL FINANCIAL STATEMENTS

Table of Contents (Continued)

Table of Contents (Continued)

Table of Contents (Continued)

CHAPTER 11

PERSONAL FINANCIAL STATEMENTS

11.000 APPLICABILITY OF SSARS

General

11.001 An accountant may be engaged to compile or review the personal financial statements of an individual, a husband and wife, or a larger family group. The basic requirements of Statement on Standards for Accounting and Review Services (SSARS) apply to these types of engagements. However, there are some unique features of engagements involving personal financial statements. This chapter focuses on those features. It also includes examples of forms that may be used to document the accountant's work, and sample financial statements and compilation and review reports.

Other Literature

11.002 The AICPA has published a *Personal Financial Statements Guide* to assist the accountant in applying professional standards to engagements involving personal financial statements. The Guide includes Statement of Position (SOP) 82-1, *Accounting and Financial Reporting for Personal Financial Statements*. The Guide and SOP contain the generally accepted accounting principles (GAAP) that should be followed in preparing personal financial statements.

Personal Financial Statements Included in Personal Financial Plans

11.003 In accordance with paragraph 7 of SSARS No. 1, an accountant should not submit unaudited personal financial statements to his or her client or others unless, as a minimum, the accountant compiles the financial statements. *There is one exception to this requirement.* SSARS No. 6 provides an exemption from SSARS No. 1 for personal financial statements included in written personal financial plans prepared by the accountant.

11.004 An accountant may submit a written personal financial plan containing unaudited personal financial statements to a client without complying with the requirements of SSARS No. 1, when all of the following conditions exist:

a. The accountant establishes an understanding with the client, preferably in writing, that the financial statements —

   1. Will be used solely to assist the client and the client's advisers to develop the client's personal financial goals and objectives, and

2. Will not be used to obtain credit or for any purposes other than developing these goals and objectives.

b. Nothing comes to the accountant's attention during the engagement that would cause the accountant to believe that the financial statements will be used to obtain credit or for any purposes other than developing these goals and objectives.

11.005 When using this exemption, the accountant should include a written report stating that the financial statements:

- Are designed solely to help develop the financial plan.
- May be incomplete or contain other departures from generally accepted accounting principles (GAAP) and should not be used to obtain credit or for any purposes other than developing the personal financial plan.
- Have not been audited, reviewed, or compiled.

A sample report for personal financial statements included in a personal financial plan is included in section 11.714.

11.006 SSARS No. 6, Interpretation No. 1, *Submitting a Personal Financial Plan to a Client's Advisers*, (AR 9600.01-.03) states that developing the client's personal financial goals and objectives encompass implementing the personal financial plan. Therefore, an accountant may submit a written personal financial plan containing unaudited personal financial statements to a client, to be used by the client or the client's advisers to implement the personal financial plan, without complying with SSARS No. 1. Examples of implementation of a personal financial plan by a client's advisers include use of the plan by —

- An insurance broker who will identify specific insurance products
- An investment adviser who will provide specific recommendations about the investment portfolio
- An attorney who will draft a will or trust documents

Personal Financial Statements on Prescribed Forms

11.007 Personal financial statements also may be presented on prescribed forms. A typical example is a financial statement form that is part of a bank loan application. When the accountant submits these types of financial statements to the client or others, he or she should compile the financial statements in accordance with SSARS No. 1. However, the accountant may find it preferable to use the alternate form of the accountant's report, as described in SSARS No. 3. The requirements of SSARS No. 3 are discussed in Chapter 10. (See section 11.710 for an illustrative report on personal financial statements in a prescribed form.)

11.100 PRESENTATION GUIDELINES FOR PERSONAL FINANCIAL STATEMENTS

11.101 The basic reporting entity for personal financial statements is an individual, a husband and wife, or a group of related individuals. Because the primary focus of personal financial statements is an individual's assets and liabilities, the only required basic financial statement is the *statement of financial condition*. This statement presents:

- Assets at their estimated current values
- Liabilities at their estimated current amounts
- Estimated income taxes on the differences between estimated current values and amounts of assets and liabilities and their tax bases
- The individual's net worth

11.102 The statement of changes in net worth is an *optional* statement. It presents the major sources of increases and decreases in net worth for a period of time, including:

a. Major sources of increases:
   - income
   - increases in the estimated current values of assets
   - decreases in the estimated current amounts of liabilities
   - decreases in the estimated income taxes

b. Major sources of decreases:
   - expenses
   - decreases in the estimated current values of assets
   - increases in the estimated current amounts of liabilities
   - increases in the estimated income taxes

11.103 The presentation of comparative financial statements of the current period and one or more prior periods may sometimes be desirable, but it is *not* required.

Other Comprehensive Bases of Accounting

11.104 Personal financial statements may be presented on other bases of accounting, such as the historical cost basis of accounting or the tax basis of accounting. In these situations, the accountant should follow the guidance in SSARS No. 1 about reporting on financial statements on some other comprehensive basis of accounting, including the following:

- The titles of the statements should be modified to indicate that they are not presented in accordance with GAAP (e.g., Statement of Assets and Liabilities — Tax Basis).

- The basis of accounting should be described in a note to the financial statements.
- The accountant's review report should be modified to indicate that the accountant is not aware of any material modifications that should be made to the statement in order for it to be in conformity with the specified other comprehensive basis of accounting.
- If the accountant compiles financial statements that omit disclosures, including disclosure of the basis of accounting, the accountant's compilation report should disclose the basis.

Chapter 9 provides a complete discussion of reporting on financial statements presented on other comprehensive bases of accounting. In addition, sections 11.711, 11.712, 11.720 and 11.721 have sample compilation and review reports for personal financial statements prepared on other comprehensive bases of accounting.

Personal Financial Statements in Accordance with GAAP

11.105 SOP 82-1 describes generally accepted accounting principles for personal financial statements. In accordance with GAAP, the statement of financial condition presents assets at their estimated current values, liabilities at their estimated current amounts, and estimated income taxes on the differences between the estimated current values and amounts of assets and liabilities and their tax bases. Assets and liabilities and changes in them are recognized on the *accrual basis*, and they are presented in the statement of financial condition in order of liquidity and maturity, without classification as current or noncurrent.

11.106 If personal financial statements are prepared for one member of a group of joint owners of an asset, the statements should include only the individual's interest as a beneficial owner, based on the property laws of the state having jurisdiction.

11.107 Business interests (including sole proprietorships, closely held corporations, and partnerships) that constitute a large part of the individual's total assets should be shown separately from other investments. The investment should be shown as a single amount representing the estimated current value of the investment, if it is marketable as a going concern. The assets and liabilities of the businesses *should not* be combined with the individual's assets and liabilities.

11.108 The estimated current value of assets and the estimated current amounts of liabilities of limited business activities not conducted in a separate business entity, should be presented as assets and liabilities of the individual. For example, if the individual owns rental real estate subject to a mortgage, the real estate would be presented as an asset at its estimated current value, and the mortgage would be presented as a liability at its estimated current amount.

Guidelines for Determining Estimated Current Values and Amounts

11.109 As indicated above, personal financial statements in accordance with GAAP present assets at their estimated current values and liabilities at their estimated current amounts. Estimated current value is defined as —

> The amount at which the asset could be exchanged between a buyer and seller, each of whom is well informed and willing, and neither of whom is compelled to buy or sell. Costs of disposal, such as commissions, if material, should be considered in determining estimated current values.

11.110 The estimated current amount of liabilities is defined as —

> The discounted amounts of cash to be paid. The discount rate should be the rate implicit in the transaction in which the debt was incurred. If the debtor is able to discharge the debt currently at a lower amount, the debt should be presented at the lower amount.

11.111 Recent transactions involving similar assets in similar circumstances ordinarily provide a satisfactory basis for determining an asset's estimated current value. If recent sales information is not available, other methods may be used, such as adjustment of historical cost based on changes in a specific price index, the use of appraisals, or the use of the discounted amounts of future cash receipts and payments. Judgment should be used to determine which method is appropriate for a particular asset.

11.112 The methods used to determine the estimated current values of assets and the estimated current amounts of liabilities should be followed consistently from period to period, unless the circumstances change.

Receivables

11.113 Receivables should be presented at the discounted amounts of cash the individual estimates will be collected, using appropriate interest rates at the date of the financial statements.

Valuation Example

If the individual has a 20-year trust deed receivable that was issued at 10% and the rate at the financial statement date is 15% for similar receivables, the estimated current value of the receivable should be computed as the discounted value of the future interest and principal payments discounted at 15%.

Practice Tip:

Often receivables may be presented at the amount of principal outstanding at the financial statement date. Discounting is only necessary when the effects are material; for example, when collection of the entire principal is not expected, or the receivable is collectible over an extended period of time and the interest rate of the receivable is significantly different from the current interest rate.

Marketable Securities

11.114 Marketable securities should include only debt and equity securities for which market quotations are available. Guidelines for determining the estimated current values are described as follows:

- The estimated current values of securities traded on securities exchanges are the closing prices of the securities on the date of the financial statement (valuation date) if the securities were traded on that date
- If the securities were not traded on the valuation date but published bid and asked prices are available, the estimated current values of the securities should be within the range of those prices
- For securities traded in the over-the-counter market with bid and asked prices from a number of sources, the mean of the bid prices, of the bid and asked prices, or of the prices of a representative selection of broker-dealers quoting the securities may be used.

11.115 The estimated current values determined by the above guidelines may have to be adjusted. For example, a large block of stock might not be salable at the price at which a small number of shares were recently sold. In addition, a large minority interest may be difficult to sell despite isolated sales of a small number of shares. Alternatively, a premium may be related to the sale of a controlling interest. Any restrictions on the transfer of a security also may suggest the need to adjust the recent market price in determining the estimated current value.

Options

11.116 If published prices of options are unavailable, their estimated current values should be determined on the basis of the assets subject to option, considering such factors as the exercise prices and the length of the option period.

Investments in Life Insurance

11.117 The estimated current value of an investment in life insurance is the cash value of the policy reduced by any policy loans. The face amount of policies owned by the individual should be disclosed.

Investments in Closely-Held Businesses

11.118 Only the net investment in a business enterprise (not its assets and liabilities) should be presented in the statement of financial condition. The net investment should be presented at its estimated current value on the financial statement date. There is no one generally accepted procedure for determining the estimated current value of an investment in a closely-held business. Methods that are commonly used are set forth as follows:

- Multiple of earnings
- Liquidation value
- Reproduction value

- Appraisals
- Discounted projected cash receipts and payments
- Book value
- Cost of the investment

If a buy-sell agreement exists, it should be considered in determining the estimated current value of the investment.

Real Estate (Including Leaseholds)

11.119 Information that may be used to determine the estimated current values of real estate and leaseholds includes the following —

- Sales of similar property in similar circumstances
- The discounted amounts of projected cash receipts and payments
- The net realizable value of the property based on planned courses of action
- Appraisals from real estate agents or brokers or those used to obtain financing
- Assessed value for property taxes, including consideration of the basis for such assessments and their relationship to market values

Intangible Assets

11.120 Intangible assets should be presented at the discounted amounts of projected cash receipts and payments arising from the planned use or sale of the assets, if both the amounts and timing can be reasonable estimated. The cost of a purchased intangible should be used if no other information is available.

Future Interest and Similar Assets

11.121 Nonforfeitable rights to receive future assets, such as pension and profit sharing benefits and annuities, should be presented at their discounted amounts if they have all of the following characteristics:

a. The rights are for fixed or determinable amounts

b. The rights are not contingent on the holder's life expectancy or the occurrence of a particular event, such as disability or death

c. The rights do not require future performance of service by the holder

11.122 Nonforfeitable rights that typically have these characteristics include —

- Guaranteed minimum portions of pensions

- Vested interests in pension and profit sharing plans
- Deferred compensation contracts
- Beneficial interests in trusts
- Remainder interests in property subject to life estates
- Annuities
- Fixed amounts of alimony for a definite period

11.123 The discounted amount of a nonforfeitable right is determined by discounting the future cash receipts at the prevailing discount rate for these types of assets at the financial statement date.

11.124 The estimated current value of an interest in a trust is determined by first estimating the cash to be received and the timing of the receipts, and then discounting these amounts using the estimated interest rate earned by the trust assets at the date of the financial statement.

Valuation Example

Assume an individual is the beneficiary of the income of a trust for his remaining life, at which time the trust assets revert to a remainderman. If the income beneficiary is in good health, and based on mortality tables, has a life expectancy of 12 more years, the estimated current value of the interest in the trust for that individual would be the discounted value of the projected annual earnings of the trust for the next 12 years discounted at the estimated earning rate of the trust assets. The remainderman's estimated current value of his interest in the trust would be computed by determining the discounted value of the trust assets to be received at the death of the income beneficiary (estimated to be in 12 years) discounted at the estimated earning rate of the trust assets. However, the remainderman should not recognize the trust interest on his statement of financial condition if he receives the assets only if he outlives the income beneficiary, because, in that case, the rights are contingent on the remainderman's life expectancy. It might be argued that this is also true for the income beneficiary. However, it is only the value of the interest that is contingent on the income beneficiary's life expectancy. That individual currently has a noncontingent right to receive income of the trust.

Payables and Other Liabilities

11.125 Payables and other liabilities should be presented in the statement of financial condition at their estimated current amounts — the discounted amounts of cash to be paid. The discount rate should be the rate implicit in the transaction in which the debt was incurred. Therefore, it is not necessary to discount the liability unless the liability was originally issued at an unrealistic interest rate. If, however, the individual is able to discharge the debt at a lower amount, the debt should be presented at the lower amount.

Practice Tip:

There is an important difference between the way receivables and payables are discounted. As indicated above, if it is necessary to discount a liability, it is discounted at the interest rate that prevailed at the time the debt was incurred. If a receivable is discounted, the prevailing interest rate at the financial statement date is used.

Noncancellable Commitments

11.126 Noncancellable commitments to pay future sums that have all of the following characteristics should be presented as liabilities at their discounted amounts:

- The commitments are for fixed or determinable amounts
- The commitments are not contingent on others' life expectancies or the occurrence of a particular event, such as disability or death
- The commitments do not require performance of future services by others

Noncancellable commitments that may have those characteristics include fixed amounts of alimony for a definite future period and pledges to charitable organizations. The interest rate prevailing at the time the commitment was executed should be used to determine the discounted amount of the liability. Significant noncancellable commitments that do not meet these requirements are disclosed in the financial statements.

Income Taxes Payable

11.127 The liability for income taxes payable should include unpaid income taxes for completed tax years and an estimated amount for income taxes accrued for the elapsed portion of the current tax year to the date of the financial statement. That estimate should be based on the relationship of taxable income earned to date to total estimated taxable income for the year, net of taxes withheld and estimated tax payments.

Estimated Income Taxes on the Differences Between the Estimated Current Values and Amounts of Assets and Liabilities and Their Tax Bases

11.128 A provision should be made for estimated income taxes on the differences between the estimated current values and amounts of assets and liabilities and their tax bases, including consideration of the negative tax bases of tax shelters. The provision should be computed as if all assets had been sold and all liabilities liquidated on the date of the financial statements, using applicable income tax laws and regulations and considering recapture provisions and available carryovers. If the individual has not reached the age of 59½ at the financial statement date, the provision should also include the special excise tax on early distribution from a qualified retirement plan. The provision should be presented between liabilities and net worth on the statement of financial condition, and all assumptions used to calculate the provision should be disclosed.

Valuation Example

The following table illustrates the computation of the estimated taxes on differences between estimated current values and amounts of assets and liabilities and their tax bases:

Description	(A) Estimated Current Value	(B) Tax Basis	Excess of (A) Over (B)	Effective Income Tax Rate	Estimated Income Taxes
Residence*	$250,000	$185,000	$ 65,000	28%	$ 18,200
Marketable Sec.	154,000	120,000	34,000	28%	9,520
R & B Corp.	500,000	325,000	175,000	28%	49,000
W & R Ltd.**	220,000	80,000	140,000	28%	39,200
Individual Retirement Account***	25,000	0	25,000	28%	7,000
					$122,920

* The tax basis of the residence was adjusted for the $125,000 exclusion, because the individual is over 55 years of age.

** The tax basis of W & R Ltd. was computed considering a passive loss carryover of $15,500.

*** The 10% special excise tax for early distribution from a retirement plan is not considered, because the individual is over 59½ years of age.

Financial Statement Disclosures

11.129 Personal financial statements should include sufficient disclosures to make the statements adequately informative. The disclosures may be made in the body of the financial statements or in the notes. The type of information typically disclosed in personal financial statements is included in the Disclosure Checklist for Personal Financial Statements in section 11.609.

11.200 ADMINISTRATION OF PERSONAL FINANCIAL STATEMENT ENGAGEMENTS

11.201 Some procedures are common to all personal financial statement engagements, including:

- A decision to accept (or continue with) the client.
- Establishing an understanding with the client regarding the nature of the services to be rendered.
- Gathering information for preparation of the statements.
- Obtaining client representation letters.

Acceptance and Continuance of Clients

11.202 Before accepting an engagement involving personal financial statements, the accountant ordinarily will evaluate acceptability of the client by considering such factors as the following:

- Facts that might bear on the integrity of the client
- Circumstances that present unusual business risk
- The accountant's ability to serve the client
- The effect of the lack of independence on the type of report that may be issued
- Whether available accounting records or other data provide a sufficient basis for providing the services requested

Because of the informal nature of most personal financial records, the accountant typically must rely more heavily on representations of management about the completeness of the financial records. Therefore, client acceptance and continuance takes on particular significance for personal financial statement engagements. Section 3.501 in Chapter 3 contains a Client Acceptance and Continuance Form that may be adapted for a personal financial statement engagement.

Establishing an Understanding with the Client

11.203 Once the accountant has decided to accept or to continue an engagement, he or she should establish an understanding with the client, preferably in writing, regarding the services to be performed and the terms and objectives of the engagement. Sample engagement letters for personal financial statement engagements are presented in sections 11.601 and 11.602.

Gathering Information

11.204 Because the financial records of individuals are often informal, only a portion of the assets and liabilities may be recorded. The accountant should consider the extent of accounting services that may have to be rendered to assist the client in gathering the information required for the financial statements. It may be necessary to obtain information from outside sources such as bankers, financial consultants, attorneys, and others who might know about the client's financial affairs. In addition, the following sources may provide information to prepare personal financial statements:

- **Checkbooks.** The individual's checkbook not only may be used as the source of the individual's cash balance, but may also serve as the primary record of cash receipts and disbursements. As such, it can provide information concerning addition or disposition of assets and creation or payment of liabilities that should be included in the statement of financial condition. For example, a real estate tax payment should lead the accountant to consider whether the related real estate is recorded as an asset and, if payment was made after the date of the financial statements, whether the liability was or should have been accrued.
- **Broker's statements.** The accountant may use statements provided to the individual by brokers as a source of information regarding marketable securities held by the client and loans that might be outstanding.
- **Property insurance policies and schedules.** The accountant may use insurance policies and schedules to consider whether the assets insured should be included in the financial statements.
- **Wills.** The accountant may use the individual's will to consider whether all assets bequeathed are included in the financial statements.
- **Leases.** The accountant may use leases to consider whether assets and liabilities related to leases are included in the financial statements.
- **Listings of vault or safe deposit box contents.** The accountant may use such listings to consider whether all assets stored and owned by the client are included in the financial statements.
- **Real estate and personal property tax returns.** The accountant may use such tax returns to consider whether all assets listed on such returns and whether all liabilities due the taxing authorities are included in the financial statements.
- **Income tax returns (and revenue agents' reports, if any).** The accountant may use income tax returns and revenue agents' reports to consider whether assets providing income and potential liabilities are recorded in the financial statements.
- **Financial records of other entities.** The accountant may use the financial statements or tax returns of separate entities, such as a closely held business, a trust, or a profit-sharing or deferred compensation plan, as sources of information regarding the client's interest in the entities.

Client Representation Letters

11.205 SSARS No. 7 includes a requirement to obtain a written representation letter for all review engagements. A sample representation letter for review engagements is included in section 11.607.

11.300 COMPILATION OF PERSONAL FINANCIAL STATEMENTS

11.301 Standards for the compilation of financial statements prescribed by SSARS No. 1 apply to personal financial statements in the same way they apply to the compilation of other types of financial statements. Accordingly, the accountant should:

1. Obtain sufficient knowledge of the accounting principles and practices applicable to personal financial statements.

2. Possess a general understanding of—

   - The nature of the individual's financial transactions,
   - The form of available accounting records,
   - The stated qualifications of accounting personnel, if any,
   - The accounting basis on which the financial statements are to be presented, and
   - The form and content of the financial statements.

3. Consider the extent of other services that might be required to assist the individual in gathering the information necessary to compile the financial statements.

4. Obtain an understanding of the methods by which the individual determined the estimated current values of significant assets and the estimated current amounts of significant liabilities and consider whether the methods are appropriate in light of the nature of each asset or liability.

5. Obtain additional or revised information if he or she becomes aware that information supplied by the individual is incorrect, incomplete, or otherwise unsatisfactory for the purpose of compiling the financial statements. If the individual refuses to provide additional or revised information, the accountant should withdraw from the compilation engagement.

6. Read the compiled personal financial statements and consider whether such statements appear to be appropriate in form and free from obvious material misstatements.

Suggested Working Papers

11.302 The following table illustrates the suggested working papers for documenting an engagement to compile personal financial statements.

Suggested Working Papers for Compilation of Personal Financial Statements

Section	Description	Page
11.601	Engagement Letter or Memorandum Describing Understanding With the Client	11-31
3.501	Client Acceptance and Continuance Form	3-23
11.603	Form for Documenting Understanding of Client—Personal Financial Statement Compilation and Review Engagements	11-35
11.604	Form for Gathering Information—Personal Financial Statements	11-39
11.605	Compilation Engagement Work Program—Personal Financial Statements	11-49
11.607	Representation Letter	11-61
11.608	Technical Review Checklist (If Required by Firm Policy)	11-63
11.609	Disclosure Checklist for Personal Financial Statements (If Statements Do Not Omit Disclosures)	11-65
11.610	Financial Statement Control Form	11-69
	Documentation of Any Other Procedures Performed or Other Special Circumstances (e.g., Step-Down to a Lower Level of Service)	

11.400 REVIEW OF PERSONAL FINANCIAL STATEMENTS

11.401 Standards for review of financial statements contained in SSARS No. 1 apply to the review of personal financial statements in the same way they apply to the review of other types of financial statements. Accordingly, the accountant should—

- Possess knowledge of the accounting principles and practices applicable to personal financial statements.
- Possess an understanding of the individual's financial activities and financial position that will provide the accountant, through the performance of inquiry and analytical procedures, with a reasonable basis for expressing limited assurance that there are no material modifications that should be made to the financial statements. This understanding should include—
  - A general understanding of the nature of the individual's assets and liabilities,
  - The sources of the individual's income, and
  - The nature of significant expenditures and material transactions with related parties.
- Perform appropriate inquiry and analytical procedures.

The Nature of Inquiry and Analytical Procedures

11.402 The accountant's inquiry and analytical procedures should ordinarily consist of—

1. Inquiries about the accounting principles and practices and methods followed in applying them, and any significant assumptions or interpretations underlying their use.
2. Inquiries concerning whether the methods and procedures for determining the estimated current values of assets and the estimated current amounts of liabilities are in accordance with those described in SOP 82-1 and are appropriate in light of the nature of each asset or liability.
3. Inquiries concerning the sources of information used in determining the estimated current values and amounts.
4. Inquiries concerning procedures for recording, classifying, and summarizing transactions, and accumulating information for disclosure in the financial statements.
5. Analytical procedures designed to identify relationships, individual items, and estimated current values and amounts that appear to be unusual. Analytical procedures might include comparison of the financial statements with statements for comparable prior periods, or study of relationships of the elements in the financial statements that would be expected to conform to a predictable pattern. For example, the accountant might examine the relationships of marketable securities and other income-producing assets to investment income, debt to interest expense, and real property to real estate taxes.

6. Consideration of whether the results of analytical procedures are consistent with responses to related inquiries.

7. Reading the financial statements to consider, on the basis of information coming to the accountant's attention, whether the financial statements appear to conform with GAAP (or other comprehensive bases of accounting [OCBOA]).

8. Applying appropriate review procedures to financial statements of entities that compose a significant portion of the individual's assets or obtaining reports from other accountants who have been engaged to audit, review, or compile financial statements of such entities. If the financial statements have only been compiled by another accountant, the accountant ordinarily will find it necessary to apply analytical procedures to the statements as a basis for using the information in the reviewed personal financial statements.

9. Inquiries of the individual concerning —

   a. whether the financial statements have been prepared in accordance with GAAP,

   b. changes in the individual's financial activities or accounting principles and practices,

   c. matters about which questions have arisen in the course of applying the foregoing procedures, and

   d. events subsequent to the date of the financial statements that would have a material effect on the financial statements.

10. Obtaining a signed client representation letter.

11.403 As discussed in sections 11.109 through 11.124, the current values of certain assets, such as receivables and real estate, may be based on projected amounts of earnings or projected cash receipts and payments. In such instances, the following additional procedures are appropriate:

- Inquire about the process by which the individual identified key factors that affect the projected data and developed assumptions for those factors.
- Inquire as to whether assumptions have been made for all key factors.
- Consider whether the assumptions appear to be appropriate for determining estimated current values of assets.

11.404 If a specialist has been engaged to determine the estimated current values of assets, the accountant should inquire about the qualifications and reputation of the specialist and the nature of the work performed.

Suggested Working Papers

11.405 The following table illustrates the suggested working papers for documentation of an engagement to review personal financial statements.

Sample Personal
Financial Statements

Suggested Working Papers for Review of Personal Financial Statements

Section	Description	Page
11.602	Engagement Letter or Memorandum Describing Understanding With the Client	11-33
3.501	Client Acceptance and Continuance Form	3-23
11.603	Form for Documenting Understanding of Client—Personal Financial Statement Compilation and Review Engagements	11-35
11.604	Form for Gathering Information—Personal Financial Statements	11-39
11.606	Review of Personal Financial Statements—Inquiries and Analytical Procedures	11-53
11.607	Representation Letter	11-61
11.608	Technical Review Checklist (If Required by Firm Policy)	11-63
11.609	Disclosure Checklist for Personal Financial Statements	11-65
11.610	Financial Statement Control Form	11-69
	Documentation of Any Other Procedures Performed or Other Special Circumstances (e.g., Step-Down to a Lower Level of Service)	

11.500 ILLUSTRATIVE PERSONAL FINANCIAL STATEMENTS

James and Jane Person
Statements of Financial Condition
December 31, 19X3 and 19X2

	December 31, 19X3	December 31, 19X2
ASSETS		
Cash	$ 3,700	$ 15,600
Bonus receivable	20,000	10,000
Investments		
Marketable securities (Note 2)	160,500	140,700
Stock options (Note 3)	28,000	24,000
Ken Bruce Associates (Note 4)	48,000	42,000
Davekar Company, Inc. (Note 5)	550,000	475,000
Vested interest in deferred profit sharing plan	111,400	98,900
Remainder interest in testamentary trust (Note 6)	171,900	128,800
Cash value of life insurance ($43,600 and $42,900), less loans payable to insurance companies ($38,100 and $37,700) (Note 7)	5,500	5,200
Residence (Note 8)	190,000	180,000
Personal effects (excluding jewelry) (Note 9)	55,000	50,000
Jewelry (Note 9)	40,000	36,500
	$1,384,000	$1,206,700
LIABILITIES		
Income taxes—current year balance	$ 8,800	$ 400
Demand 10.5% note payable to bank	25,000	26,000
Mortgage payable (Note 10)	98,200	99,000
Contingent liabilities (Note 11)	—	—
	132,000	125,400
Estimated income taxes on the differences between the estimated current values assets and the estimated current amounts of liabilities and their tax bases (Note 12)	239,000	160,000
NET WORTH	1,013,000	921,300
	$1,384,000	$1,206,700

See accompanying notes and accountant's review report.

James and Jane Person
Statements of Changes in Net Worth
Years Ended December 31, 19X3 and 19X2

	Year ended December 31,	
	19X3	19X2
Realized increases in net worth		
Salary and bonus	$ 95,000	$ 85,000
Dividends and interest income	2,300	1,800
Distribution from limited partnership	5,000	4,000
Gains on sales of marketable securities	1,000	500
	103,300	91,300
Realized decreases in net worth		
Income taxes	26,000	22,000
Interest expense	13,000	14,000
Real estate taxes	4,000	3,000
Personal expenditures	36,700	32,500
	79,700	71,500
Net realized increase in net worth	23,600	19,800
Unrealized increases in net worth		
Marketable securities (net of realized gains on securities sold)	3,000	500
Stock option	4,000	500
Davekar Company, Inc.	75,000	25,000
Ken Bruce Associates	6,000	
Deferred profit sharing plan	12,500	9,500
Remainder interest in testamentary trust	43,100	24,800
Jewelry	3,500	200
	147,100	60,500
Unrealized decrease in net worth		
Estimated income taxes on the differences between the estimated current values of assets and the estimated current amounts of liabilities and their tax bases	79,000	22,000
Net unrealized increase in net worth	68,100	38,500
Net increase in net worth	91,700	58,300
Net worth at the beginning of year	921,300	863,000
Net worth at the end of year	$1,013,000	$ 921,300

See accompanying notes and accountant's review report.

James and Jane Person
Notes to Financial Statements

Note 1 — Basis of Accounting

The accompanying financial statements include the assets and liabilities of James and Jane Person. Assets are stated at their estimated current values and liabilities at their estimated current amounts.

Note 2 — Marketable Securities

The estimated current values of marketable securities are either (a) their quoted closing prices or (b) for securities not traded on the financial statement date, amounts that fall within the range of quoted bid and asked prices.

Marketable securities consist of the following:

	December 31, 19X3		December 31, 19X2	
	Number of shares or bonds	Estimated Current Values	Number of shares or bonds	Estimated Current Values
Stocks	11,500	$ 98,813		
Jaiven Jewels, Inc.	800	11,000	600	$ 4,750
McRae Motors, Ltd.	400	13,875	200	5,200
Parker Sisters, Inc.			1,200	96,000
Rosenfield Rug Co.	300	9,750	100	2,875
Rubin Paint Company				
Weiss Potato Chips, Inc.	200	20,337	300	25,075
		153,775		133,900
Bonds				
Jackson Van Ltd. (12% due 7/1/X9)	5	5,225	5	5,100
United Garvey, Inc. (7% due 9/15/X6)	2	1,500	2	1,700
		6,725		6,800
		$160,500		$140,700

Note 3 — Options

Jane Person owns an option to acquire 4,000 shares of stock of Winner Corp. at an option price of $5 per share. The option expires on June 30, 19X5. The estimated current value is its published selling price.

Note 4 — Ken Bruce Associates

The investment in Ken Bruce Associates is an 8% interest in a real estate limited partnership. The estimated current value is determined by the projected annual cash receipts and payments capitalized at a 12% rate.

Note 5 — Davekar Company, Inc.

James Person owns 50% of the common stock of Davekar Company, Inc., a retail mail order business. The estimated current value of the investment is determined by the provisions of a shareholders' agreement, which restricts the sale of the stock and, under certain conditions, requires the company to repurchase the stock based on a price equal to the book value of the net assets plus an agreed amount for goodwill. At December 31, 19X3, the agreed amount for goodwill was $112,500, and at December 31, 19X2, it was $100,000.

Condensed balance sheets of Davekar Company, Inc., prepared in conformity with generally accepted accounting principles, are summarized below:

	December 31,	
	19X3	19X2
Current assets	$3,147,000	$2,975,000
Plant, property, and equipment—net	165,000	145,000
Other assets	120,000	110,000
Total assets	3,432,000	3,230,000
Current liabilities	2,157,000	2,030,000
Long-term liabilities	400,000	450,000
Total liabilities	2,557,000	2,480,000
Equity	$ 875,000	$ 758,000

The sales and net income for 19X3 were $10,500,000 and $125,000 and for 19X2 were $9,700,000 and $800,000.

Note 6 — Remainder Interest

Jane Person is the beneficiary of a remainder interest in a testamentary trust under the will of the late Joseph Jones. The amount included in the accompanying statements is her remainder interest in the estimated current value of the trust assets, discounted at 10%.

Note 7 — Life Insurance

At December 31, 19X3 and 19X2, James Person owned a $300,000 whole life insurance policy.

Note 8 — Residence

The estimated current value of the residence is its purchase price plus the cost of improvements. The residence was purchased in December, 19X1, and improvements were made in 19X2 and 19X3.

Note 9 — Personal Effects and Jewelry

The estimated current values of personal effects and jewelry are the appraised values of those assets, determined by an independent appraiser for insurance purposes.

Note 10 — Mortgage Payable

The mortgage (collateralized by the residence) is payable in monthly installments of $815 a month, including interest at 10% a year through 20Y8.

Note 11 — Contingent Liabilities

James Person has guaranteed the payment of loans of Davekar Company, Inc., under a $500,000 line of credit. The loan balance was $300,000 at December 31,19X3, and $400,000 at December 31,19X2.

Note 12 — Estimated Income Taxes

The estimated current amounts of liabilities at December 31, 19X3, and December 31, 19X2, equaled their tax bases. Estimated income taxes have been provided on the excess of the estimated current values of assets over their tax bases as if the estimated current values of the assets had been realized on the statement date, using applicable tax laws and regulations. The provision will probably differ from the amounts of income taxes that eventually might be paid because those amounts are determined by the timing and the method of disposal or realization and the tax laws and regulations in effect at the time of disposal or realization.

The estimated current values of assets exceeded their tax bases by $850,000 at December 31, 19X3, and by $770,300 at December 31, 19X2. The excess of estimated current values of major assets over their tax bases are:

	December 31,	
	19X3	19X2
Investment in Davekar Company, Inc.	$ 430,500	$ 355,500
Vested interest in deferred profit sharing plan	111,400	98,900
Investment in marketable securities	104,100	100,000
Remainder interest in testamentary trust	97,000	53,900

Documentation — PFS

11.600 DOCUMENTATION FOR PERSONAL FINANCIAL STATEMENT ENGAGEMENTS

11.601 Engagement Letter — Compilation of Personal Financial Statements

____
____
____

This letter is to confirm my (our) understanding of the terms and objectives of my (our) engagement and the nature and limitations of the services we will provide.

I (We) will perform the following services:

- I (We) will compile, from information you provide, the statement of financial condition of ____________________________ [client's name] as of __________________ [statement of financial condition date], (and the related statement of changes in net worth for the ___________ [period] then ended). We will not audit or review such financial statement(s). My (Our) standard report on the compilation of your financial statements reads as follows:

  I (We) have compiled the accompanying statement of financial condition of ________________________________ [client's name] as of __________ [statement of financial condition date], (and the related statement of changes in net worth for the ___________ [period] then ended), in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

  A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statement(s) are presented. I (We) have not audited or reviewed the accompanying financial statement(s) and, accordingly, do not express an opinion or any other form of assurance on it (them).

  If, for any reason, I am (we are) unable to complete my (our) compilation of your financial statement(s), I (we) will not issue a report on such statement(s) as a result of this engagement.

- I (We) will also perform additional accounting services to enable you to develop sufficient accounting records to provide a basis for the compiled financial statement(s). Performing these additional accounting services does not alter the fact that you are responsible for the information contained in the financial statement(s), including the values and amounts assigned to the assets and liabilities, (and we will require a client representation letter from you).

  My (Our) engagement cannot be relied upon to disclose errors, irregularities, or illegal acts, including fraud or defalcations, that might exist. However, I (we) will inform you of material errors, and any irregularities or illegal acts that come to my (our) attention, unless they are clearly inconsequential.

My (Our) fees will be billed as work progresses and are based on the amount of time required plus out-of-pocket expenses. Invoices are payable upon presentation. I (We) will notify you immediately of any circumstances I (we) encounter that could significantly affect my (our) initial estimate of total fees, which will range from $__________ to $__________.

If this letter correctly expresses your understanding, please sign the enclosed copy where indicated and return it to me (us).

I (We) appreciate the opportunity to serve you and trust that our association will be a long and pleasant one.

Sincerely,

____
[Engagement Partner's Signature]

____
[Date]

Accepted and agreed to:

____
[Client Representative's Signature]

____
[Title]

____
[Date]

11.602 Engagement Letter — Review of Personal Financial Statements

____

____

____

This letter is to confirm my (our) understanding of the terms and objectives of my (our) engagement and the nature and limitations of the services I (we) will provide.

I (We) will perform the following services:

- I (We) will review the statement of financial condition of ____________________ [client's name] as of ____________ [statement of financial condition date], (and the related statement of changes in net worth for the __________ [period] then ended), in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. My (Our) review will consist primarily of inquiries of you and analytical procedures applied to financial data, and I (we) will require a client representation letter from you. A review does not contemplate obtaining an understanding of the internal control structure or assessing control risk, tests of accounting records and responses to inquiries by obtaining corroborating evidential matter, and certain other procedures ordinarily performed during an audit. Thus, a review does not provide assurance that I (we) will become aware of all significant matters that would be disclosed in an audit. My (Our) engagement cannot be relied upon to disclose errors, irregularities, or illegal acts, including fraud or defalcations, that may exist. However, I (we) will inform you of material errors, and any irregularities or illegal acts that come to my (our) attention, unless they are clearly inconsequential.

  I (We) will not perform an audit of such financial statement(s), the objective of which is the expression of an opinion regarding the financial statement(s) taken as a whole, and accordingly, I (we) will not express such an opinion on them (it).

  My (Our) standard form review report reads as follows:

  > I (We) have reviewed the accompanying statement of financial condition of ______________________ [client's name] as of __________________ [statement of financial condition date], (and the related statement of changes in net worth for the __________ [period] then ended), in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statement(s) is the representation of __________________ [client's name].
  >
  > A review of personal financial statements consists principally of inquiries of the individuals whose financial statements are presented and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statement(s) in order for it (them) to be in conformity with generally accepted accounting principles.

- I (We) will also perform additional accounting services to enable you to develop sufficient accounting records to provide a basis for the reviewed financial statement(s). Performing these additional accounting services does not alter the fact that you are responsible for the information contained in the financial statement(s), including the values and amounts assigned to the assets and liabilities.

My (Our) fees will be billed as work progresses and are based on the amount of time required plus out-of-pocket expenses. Invoices are payable upon presentation. I (We) will notify you immediately of any circumstances I (we) encounter that could significantly affect my (our) initial estimate of total fees, which will range from $_________ to $_________.

If this letter correctly expresses your understanding, please sign the enclosed copy where indicated and return it to me (us).

I (We) appreciate the opportunity to serve you and trust that our association will be a long and pleasant one.

Sincerely,

____

[Engagement Partner's Signature]

____

[Date]

Accepted and agreed to:

____

[Client Representative's Signature]

____

[Title]

____

[Date]

11.603

Form for Documenting Understanding of Client — Personal Financial Statement Compilation and Review Engagements

Client: ______________________________

Financial Statement Date: ______________________________

INSTRUCTIONS:

This form should be completed or updated for all personal financial statement engagements. The form provides documentation of the required understanding of the client.

1. Identify the nature of the financial statement entity.

   a. Individual ☐
   b. Husband and wife ☐
   c. Larger family group ☐

   Describe the entity.

2. If the individual (family) has (have) significant assets owned jointly with other individuals, describe the manner in which the separate assets and liabilities will be determined.

3. Describe the major sources of revenues for the individual or family.

4. Describe any unusual assets or liabilities owned by the individual or family.

5. Describe any assets or liabilities that will present difficult valuation problems.

6. Describe the nature of the personal accounting records.

7. Identify who maintains the personal accounting records and describe that individual's qualifications.

8. Describe the client's procedures for recording, classifying, and summarizing transactions and accumulating information for disclosure in the financial statements.

9. Identify the accounting basis for the financial statements, e.g., GAAP, tax, or historical cost basis.

	19__	19__	19__	19__	19__	19__	19__
Prepared or Updated by:	___	___	___	___	___	___	___
Reviewed by (Partner):	___	___	___	___	___	___	___

11.604

Form for Gathering Information — Personal Financial Statements

Client: ______________________________

Financial Statement Date: ______________________________

INSTRUCTIONS:

This form may be used to gather information for engagements to compile or review personal financial statements.

ASSETS

Cash

Financial Institution	Type of Account	Restricted?	Reconciled Balance
		Yes No	$
		Yes No	
		Yes No	
		Yes No	
		Yes No	
Total			$

Describe any restrictions of cash balances:

Marketable Securities

Describe the securities below or attach a copy of the broker's listing with the additional information added.

Description of Security (Including No. of Units)	Date Acquired	Market Price Per Unit	Total Cost (Tax Basis)	Total Market Value
		$	$	$
Total			$	$

Describe the sources of market values of securities:

If the client has a cash account or margin account with the broker, include the cash balance or loan in the appropriate section of this form.

Receivables

Debtor's Name	Due Date	Int. Rate	Estimated Principal to be Collected	Tax Basis	Estimated Current Value
			$	$	$
Total				$	$

Use the estimated principal to be collected as the estimated current value unless the receivable is long-term and its interest rate differs significantly from the current interest rate. In those situations, the receivable should be discounted using the prevailing interest rate at the financial statement date.

Describe any other terms of the receivables:

Options

Description	Tax Basis	Value
	$	$
	$	$

Investments in Life Insurance

Insurance Company	Owner	Face Amt.	Cash Surrender Value	Estimated Current Value
		$	$	$
Total		$	$	$

The estimated current value is the cash surrender value reduced by any policy loans.

Investments in Closely Held Businesses

Name of Business			
Type of Entity (e.g., part, corp., etc.)			
Nature of the Business			
Ownership Percentage			
Tax Basis of the Client's Interest	$	$	$
Estimated Current Value of the Interest	$	$	$

Attach a copy of the financial statements of each business and the accountant's report to be used to prepare note disclosure of summarized financial data.

Real Estate

	Parcel A	Parcel B	Parcel C	Total
Location				
Type				
Ownership Percentage				
Tax Basis of Interest	$	$	$	$
Estimated Current Value of Interest	$	$	$	$

Primary Mortgage Holder				
Current Balance	$	$	$	$
Interest Rate				
Monthly Payment	$	$	$	$
Date of Last Scheduled Payment				

	Parcel A	Parcel B	Parcel C	Total
Second Mortgage Holder				
Current Balance	$	$	$	$
Interest Rate				
Monthly Payment	$	$	$	$
Date of Last Scheduled Payment				

Residences

Primary:
Location: ____________________ Square Footage: ____________________

Tax Basis: $ ____________________ Estimated Current Value: $ ____________________

Secondary:
Location: ____________________ Square Footage: ____________________

Tax Basis: $ ____________________ Estimated Current Value: $ ____________________

Mortgages on Primary Residence	First	Second	Total
Mortgage Holder			
Current Balance	$	$	$
Interest Rate			
Monthly Payment	$	$	$
Date of Last Scheduled Payment			

Mortgages on Secondary Residence	First	Second	Total
Mortgage Holder			
Current Balance	$	$	$
Interest Rate			
Monthly Payment	$	$	$
Date of Last Scheduled Payment			

Future Interests:

Nonforfeitable rights to receive future sums should be presented as assets at their discounted amounts if the rights: (1) are for fixed or determinable amounts, (2) are not contingent on the holder's life expectancy or the occurrence of a particular event, and (3) do not require future performance of services by the holder.

Description of the Interest	Tax Basis	Discounted Present Value
	$	$
Total	$	$

Other Assets:

Automobiles:

Description	Tax Basis	Estimated Current Value
	$	$
Total	$	$

Personal Effects:

Description	Tax Basis	Estimated Current Value
	$	$
Total	$	$

Other:

Description	Tax Basis	Estimated Current Value
	$	$
Total	$	$

LIABILITIES

Notes Payable

Payable To	Interest Rate	Collateral	Monthly Payment	Last Scheduled Payment	Current Amount
			$		$
Total					$

Credit Card and Accrued Payables

Payable To	Description	Current Amount
		$
Total		$

Income Taxes Payable

Estimated taxes for the current year	$
Amounts due from prior years and additional assessments	
Total taxes	
Less: Taxes withheld and estimated payments	
Income Taxes Payable	$

Estimated Taxes on Differences Between Estimated Current Values and Amounts of Assets and Liabilities and Their Tax Bases

Asset or Liability	(A) Estimated Current Values	(B) Tax Bases	Excess of (A) over (B)	Effective Income Tax Rates	Amount of Estimated Income Taxes
	$	$	$	$	$
Total					$

Assumptions used in computing estimated income taxes:

Prepared by: ______________________ Date: ______________
(In-Charge)

Reviewed by: ______________________ Date: ______________
(Partner)

11.605

Compilation Engagement Work Program — Personal Financial Statements

Client: ______________________________

Financial Statement Date: ______________________________

INSTRUCTIONS:

The following is a general guide for compiling annual and interim personal financial statements. Any additional inquiries or procedures performed, and conclusions reached, should also be documented in the working papers. The "N/A" column should be initialed for any steps that are not applicable or for steps not required because of immateriality or other reasons. References preceded by "AR" refer to *Statements on Standards for Accounting and Review Services* included in Volume 2 of the AICPA *Professional Standards*.

	Performed By		
	Initials	Date	N/A
1. Consider whether the engagement should be accepted.	______	______	☐
2. Consider whether the CPA firm is independent of the client. If the firm is not independent, the compilation report should be modified to indicate that fact. (AR 100.22)	______	______	☐
3. Establish or update an understanding with the client, preferably in writing, regarding the nature of the engagement. Include in the working papers a copy of the engagement letter or a memorandum describing the oral arrangements. (AR 100.08)	______	______	☐
4. If the firm was originally engaged to perform a higher level of service, i.e., a review or audit, document the appropriateness of the decision to step-down, including a consideration of:	______	______	☐
a. The reason given for the client's request, particularly the implications of a restriction on the scope of the			

	Performed By		
	Initials	**Date**	**N/A**
initial engagement, whether imposed by the client or by circumstances.	________	________	☐
b. The additional effort required to complete the initial engagement.	________	________	☐
c. The estimated additional cost to complete the initial engagement. (AR 100.44-.49).	________	________	☐
5. Consider whether the staffing and scheduling of the engagement is appropriate.	________	________	☐
6. Complete or update the Form For Documenting Understanding of Client—Personal Financial Statement Compilation and Review Engagements.	________	________	☐
7. Obtain assurances about the independence of any other accountants engaged to perform segments of the engagement.	________	________	☐
8. Perform any accounting services required to compile the financial statements. (AR 100.11)	________	________	☐
9. Consider whether any information supplied by the client appears to be incorrect, incomplete, or otherwise unsatisfactory. If so, request revised information. (AR 100.12)	________	________	☐
10. Draft the financial statements and the compilation report.	________	________	☐
11. If the financial statements do not omit substantially all disclosures, complete the Disclosure Checklist For Personal Financial Statements.	________	________	☐
12. If the financial statements are prepared on some other comprehensive basis of accounting, consider whether the financial statement titles and disclosure of the basis of accounting are appropriate. (AR 100.19-.21)	________	________	☐
13. Read the financial statements and consider whether they appear to be appropriate in form and free from obvious material misstatements. (AR 100.13)	________	________	☐

	Performed By		
	Initials	Date	N/A
14. If the financial statements omit substantially all disclosures required by generally accepted accounting principles (GAAP) or an other comprehensive basis of accounting (OCBOA), add an additional paragraph to the compilation report disclosing the omission. (AR 100.19-.21)	________	________	☐
15. If the financial statements contain a departure from GAAP or OCBOA, including either a measurement or disclosure departure:			
a. Revise the financial statements or modify the compilation report to indicate the departure.	________	________	☐
b. If the financial statements are not revised, consider whether modification of the standard report is adequate to indicate the deficiencies in the financial statements.	________	________	☐
c. If modification of the report is not considered adequate, consider withdrawing from the engagement. (AR 100.39-.41)	________	________	☐
16. If the financial statements are presented with comparative financial statements for one or more prior periods, determine that all financial statements are appropriately reported on by the CPA firm or a predecessor CPA firm. (AR 200.01-.36)	________	________	☐
17. If financial statements that are presented in a prescribed form are being reported on in accordance with SSARS No. 3, determine that the report complies with the requirements of that Statement. (AR 300.01-.05)	________	________	☐
18. If supplementary data accompanies the financial statements, modify the compilation report to include the other data. (AR 100.43)	________	________	☐
19. Include a reference to the compilation report on each page of the financial statements and supplementary data. (AR 100.16)	________	________	☐
20. Date the compilation report as of the date the compilation was completed. (AR 100.15)	________	________	☐

	Performed By Initials	Performed By Date	N/A
21. Document any other procedures performed or unusual problems and their resolution.	________	________	☐
22. Obtain a representation letter from the individual(s).	________	________	☐
23. Determine that all required forms and checklists have been completed.	________	________	☐
24. Determine that all review points by the engagement team and the technical reviewer (if applicable) have been resolved.	________	________	☐

Prepared by: ______________________________ Date: ______________________
(In-Charge)

Reviewed by: ______________________________ Date: ______________________
(Partner)

11.606

Review of Personal Financial Statements — Inquiries and Analytical Procedures

Client: ______________________________

Financial Statement Date: ______________________________

INSTRUCTIONS:

This form may be used to document the inquiries and analytical procedures performed in the review of personal financial statements.

PART I—INQUIRIES

General	Yes	No	N/A
1. If the statements are presented for an individual that owns joint assets do they include only the individual's interest as a beneficial owner as determined by applicable agreements and state property laws?	☐	☐	☐
2. Are assets and liabilities presented on the accrual basis?	☐	☐	☐
3. Are the methods and procedures used to determine the estimated current values of assets and the estimated current amounts of liabilities in conformity with SOP 82-1?	☐	☐	☐
4. Are significant assumptions and interpretations underlying the measurement or presentation of the financial statements reasonable?	☐	☐	☐
5. Have sufficient pertinent sources of information about the assumptions been considered, including key factors expected to materially affect the estimated current values and amounts?	☐	☐	☐
6. Are the assumptions consistent with the sources of information from which they have been derived and with each other?	☐	☐	☐
7. Was historical financial information used in developing the assumptions reliable?	☐	☐	☐

	Yes	No	N/A
8. Are the methods used to determine estimated current values of assets and estimated current amounts of liabilities consistent with those of the preceding period?	☐	☐	☐
9. If a specialist was engaged to determine the estimated current values of assets:			
a. Are the specialist's qualifications and reputation appropriate?	☐	☐	☐
b. Is the nature of the specialist's work appropriate?	☐	☐	☐
Cash			
1. Have all significant bank accounts been reconciled with checkbook balances?	☐	☐	☐
2. Has cash on hand, if significant, been counted?	☐	☐	☐
Receivables			
1. Is only the amount estimated to be collectible considered in determining the estimated current value of receivables?	☐	☐	☐
2. If necessary, have receivables been discounted to their net present value using appropriate interest rates at the financial statement date?	☐	☐	☐
3. Are there any receivables from related parties?	☐	☐	☐
Marketable Securities			
1. Do marketable securities include only debt and equity securities for which market quotations are available?	☐	☐	☐
2. Have the following guidelines been used to determine the estimated current values of marketable securities?	☐	☐	☐
a. For securities traded on exchanges, the closing price on the last business day prior to the financial statement date, if they were traded on that date.	☐	☐	☐
b. For those not traded on that date, a price that falls within the bid and asked price range on that date.	☐	☐	☐

	Yes	No	N/A
c. For securities traded in the over-the-counter market, (1) the mean of the bid prices, (2) the mean of the bid and asked prices, or (3) the mean of a representative selection of broker-dealers quoting the securities.	☐	☐	☐
3. In determining the price to use for the estimated current value was consideration given to factors such as any restrictions on transfer, the size of the block of stock, and whether it is a controlling or minority interest?	☐	☐	☐
4. Have costs of disposal been considered in determining the estimated current value of the securities?	☐	☐	☐
5. Has investment income been accrued?	☐	☐	☐

Options

	Yes	No	N/A
1. If quoted prices are not available, have estimated current values been determined based on the values of the assets subject to option?	☐	☐	☐
2. If quoted prices are not available, has consideration been given to exercise price and the length of the option period?	☐	☐	☐

Investment in Life Insurance

	Yes	No	N/A
1. Has the estimated current value of an investment in life insurance been determined as the cash value of the policy reduced by the amount of loans against it?	☐	☐	☐

Investments in Closely Held Businesses

	Yes	No	N/A
1. Is only the net investment in the business presented?	☐	☐	☐
2. Have appropriate methods been used to determine the estimated current values of the businesses?	☐	☐	☐
3. Has consideration been given to any buy-sell agreements and have the details been disclosed?	☐	☐	☐
4. Have recent appraisals or valid offers, if any, been considered?	☐	☐	☐

	Yes	No	N/A
Investments in Real Estate (including Leaseholds)			
1. Have appropriate methods been used to determine the estimated current values of the investments?	☐	☐	☐
2. Are there any unrecorded sales, disposals, or abandonments?	☐	☐	☐
Intangible Assets			
1. Are intangible assets presented at the discounted amounts of projected cash receipts and payments from the planned use of the assets?	☐	☐	☐
Future Interests and Similar Assets			
1. Are all nonforfeitable rights to receive future sums that (a) are fixed or determinable in amount, (b) are not contingent on the holder's life or occurrence of a particular event, and (c) do not require future performance presented as assets at their discounted present amounts?	☐	☐	☐
2. Is the discount rate used reasonable?	☐	☐	☐
Payables and Other Liabilities			
1. Have all significant payables been recorded?	☐	☐	☐
2. Are there any payables to related parties?	☐	☐	☐
3. Has there been compliance with restrictive covenants of loan agreements?	☐	☐	☐
4. Have amounts to be paid been discounted at an appropriate rate (i.e., the rate implicit in the transaction in which the debt was incurred)?	☐	☐	☐
5. If the debt can be discharged at a lower amount, is the debt presented at the lower amount?	☐	☐	☐
Income and Other Taxes			
1. Have provisions been made for the current and prior year's federal, state, and local tax liabilities?	☐	☐	☐
2. Have tax assessments and tax examinations in progress been considered?	☐	☐	☐

	Yes	No	N/A
3. Has a provision been made for estimated income taxes on the differences between estimated current values and amounts of assets and liabilities and their tax bases?	☐	☐	☐

Commitments and Contingencies

	Yes	No	N/A
1. Are there any contingent liabilities such as discounted notes, drafts, endorsements, litigation or unsettled asserted claims?	☐	☐	☐
2. Are there any potential unasserted claims?	☐	☐	☐
3. Are there any material contractual obligations for construction or purchase of real property or other assets?	☐	☐	☐
4. Are there any commitments or options to purchase or sell securities?	☐	☐	☐
5. Are noncancellable commitments to pay future sums meeting the criteria for recognition presented as liabilities at their discounted amounts?	☐	☐	☐

Income and Expenses

	Yes	No	N/A
1. Have salaries, bonuses, investment income, distributions from partnerships, and other income been recognized in the appropriate period?	☐	☐	☐
2. Have personal expenditures and expenses been recognized in the appropriate period?	☐	☐	☐

Other Inquiries

____

____

____

____

____

____

PART II—ANALYTICAL PROCEDURES

	Performed By		
	Initials	N/A	Comments
1. Compare dividend and interest income to the amount of marketable securities.			
________	____	☐	________
________	____	☐	________
2. Compare interest income on receivables to the balance of receivables.			
________	____	☐	________
________	____	☐	________
3. Analytical procedures applied to the financial data of closely held businesses:			
a. Comparisons to amounts from prior years.	____	☐	________
b. Ratio analysis.	____	☐	________
________ ________ ________ ________	____	☐	________
4. Test reasonableness of the net investment in closely held businesses by performing the following procedures:			
a. Compare the estimated current value to the book value.	____	☐	________
b. Compare the estimated current value to the normalized earnings of the business.	____	☐	________

	Performed By		
	Initials	N/A	Comments
c. Other: __________ __________ __________ __________	____	☐	________
5. Compare the estimated current value of real estate to tax values.	____	☐	________
6. Test the reasonableness of income producing real estate by comparing the estimated current value to the annual income.	____	☐	________
7. Test the reasonableness of real estate by computing the value per acre or square foot.	____	☐	________
8. Compare interest expense to outstanding debt.	____	☐	________
9. Other procedures: __________ __________ __________ __________ __________ __________	____	☐	________

Prepared by: ____________________ Date: ____________
(In-Charge)

Reviewed by: ____________________ Date: ____________
(Partner)

11.607 Representation Letter—Review Engagements

[Date of Accountant's Report]

[To the Accountant]

In connection with your review of the statement of financial condition of ________________ [client's name] as of __________________ [financial statement date] (and the related statement of changes in net worth and for the [period] then ended) for the purpose of __________________ [description], I (we) confirm, to the best of my (our) knowledge and belief, the following representations made to you during your review.

1. I am (We are) responsible for the fair presentation in the statement(s) of financial condition (and changes in net worth) in conformity with generally accepted accounting principles. All assets are presented at their estimated current values and all liabilities are presented at their estimated current amounts, which have been determined in accordance with guidelines promulgated by the American Institute of Certified Public Accountants. (Because of my (our) limited expertise with generally accepted accounting principles, including financial statement disclosures, I (we) have engaged you to advise me (us) in fulfilling that responsibility.)

2. I (We) have made all financial records and related data available to you. I (We) have not knowingly withheld from you any financial records or related data that in my (our) judgment would be relevant to your review.

3. The following have been properly recorded or disclosed in the financial statement(s):

   a. Related party transactions and related amounts receivable or payable, including sales, purchases, loans, transfers, leasing arrangements, and guarantees. I (We) understand that related parties include members of my (our) family as well as business entities in which I (we), or members of my (our) family, have an investment that allows the exercise of control or significant influence.

   b. Arrangements with financial institutions involving compensating balances or other arrangements involving restrictions on cash balances and line-of-credit or similar arrangements.

   c. Agreements to repurchase assets previously sold.

4. There are no violations or possible violations of laws or regulations that have come to my (our) attention whose effects are regarded as significant enough to be considered for disclosure in the financial statement(s) or as a basis for recording a loss contingency, and there are no other material liabilities or gain or loss contingencies that are required to be accrued or disclosed.

5. There are no material transactions or balances that have not been properly recorded or disclosed in the financial statement(s).

6. I (We) have satisfactory title to all owned assets, and there are no liens or encumbrances on such assets nor have any assets been pledged.

7. I (We) have not retained an attorney for matters that may involve current or potential litigation, and I am (we are) not aware of any pending or threatened litigation, claims, or assessments that should be disclosed in the financial statement(s).

8. I (We) have complied with all aspects of contractual agreements that would have a material effect on the financial statement(s) in the event of noncompliance.

9. No events have occurred subsequent to the date of the statement of financial condition that would require adjustment to, or disclosure in, the financial statement(s).

10. I (We) have responded fully to all inquiries made to me (us) by you during the engagement.

____

____

[Client's Signatures]

11.608

Technical Review Checklist

Client: ______________________________

Financial Statement Date: ______________________________

Technical Reviewer: ______________________ Date: ____________

INSTRUCTIONS:

This checklist should be completed by the technical reviewer on those engagements in which a technical review is required by the firm's quality control policies and procedures.

	Initials
1. Review the financial statements for appropriate form and content. Consider the appropriateness of:	______
a. Titles.	______
b. Captions.	______
c. Classifications within captions.	______
d. Descriptions.	______
e. Reference to auditor's (accountant's) report and financial statement notes.	______
2. Compare the Financial Statement Disclosure Checklist to the notes to the financial statements. Consider whether the notes are complete and worded appropriately.	______
3. Review the financial statements for any obvious departures from GAAP or OCBOA.	______
4. Read the auditor's (accountant's) report for appropriateness and conformity with professional standards.	______
5. If applicable, review the engagement checklists:	
a. To determine that they support the conclusions reached in the engagement.	______
b. For potential problems.	______
6. Describe any problems noted and the way they were resolved.	______

____

____

____

11.609

Disclosure Checklist for Personal Financial Statements

Client: ______________________________

Financial Statement Date: ______________________________

INSTRUCTIONS:

This form may be used to review the financial statement disclosures in reviewed or compiled personal financial statements. The source for these disclosures is paragraph 31 of SOP 82-1 (Appendix E of the *Personal Financial Statements Guide*).

	Yes	No	N/A
1. Is the individual or family unit covered by the financial statements clearly indicated?	☐	☐	☐
2. Is the fact that assets are presented at their estimated current values and liabilities at their estimated current amounts disclosed?	☐	☐	☐
3. Are the methods used in determining the estimated current values and amounts of major assets and liabilities disclosed?	☐	☐	☐
4. Are changes in the methods used from the prior period disclosed?	☐	☐	☐
5. If assets are held jointly by the individual and others, is the nature of the joint ownership disclosed?	☐	☐	☐
6. Are significant restrictions on the availability of cash balances disclosed?	☐	☐	☐
7. Are related party receivables or payables disclosed?	☐	☐	☐
8. Are receivables pledged, discounted or factored disclosed?	☐	☐	☐
9. Are marketable securities pledged or restricted disclosed?	☐	☐	☐

	Yes	No	N/A
10. If the client's investment portfolio is material in relation to his or her other assets and is concentrated in one or a few companies or industries, are the names of the companies or industries disclosed?	☐	☐	☐
11. If the client has a material investment in a closely held business, do the financial statements disclose:			
a. The name of the company?	☐	☐	☐
b. The percentage of ownership?	☐	☐	☐
c. The nature of the business?	☐	☐	☐
d. Summarized financial information about assets, liabilities, and results of operations for the most recent year based on the financial statements of the business?	☐	☐	☐
e. The basis of presentation of the summarized financial data?	☐	☐	☐
12. Are nonforfeitable rights not having the characteristics of future interests or similar assets disclosed?	☐	☐	☐
13. Are intangible assets described, along with their useful lives?	☐	☐	☐
14. Is the face amount of life insurance owned by the client disclosed?	☐	☐	☐
15. Is the following tax information disclosed?	☐	☐	☐
a. Methods and assumptions used to compute estimated income taxes on the differences between the estimated current values and amounts of assets and liabilities and their tax bases.	☐	☐	☐
b. A statement that the provision will probably differ from the amounts of income taxes that might eventually be paid because those amounts are determined by the timing and the method of disposal, realization, or liquidation and the tax laws and regulations in effect at the time.	☐	☐	☐
c. Operating and capital loss carryovers.	☐	☐	☐
d. Unused deductions and credits, including their expiration dates.	☐	☐	☐

	Yes	No	N/A
e. Differences between the estimated current values and amounts of major assets and liabilities and their tax bases.	☐	☐	☐
16. Are maturity dates, interest rates, collateral, and other pertinent details about receivables and debt disclosed?	☐	☐	☐
17. Are material contractual obligations for construction or purchase of real property or other assets disclosed?	☐	☐	☐
18. Are commitments or options to purchase or sell securities disclosed?	☐	☐	☐
19. Are commitments to pay future sums not meeting the criteria for recognition as liabilities disclosed?	☐	☐	☐
20. Are significant contingent liabilities, such as endorsements, litigation, and claims disclosed?	☐	☐	☐

Prepared by: ______________________ Date: ______________
(In-Charge)

Reviewed by: ______________________ Date: ______________
(Partner)

11.610

Financial Statement Control Form

Client: ____________________

Financial Statement Date: ____________________

INSTRUCTIONS:

This Form should be prepared by the in-charge to accompany the draft of the financial statements and report. Each step should be initialed and dated as it is completed, or checked "N/A." Step 8 must be initialed and dated by the engagement partner to release the financial statements and report.

SERVICE PERFORMED:

Compilation ☐

Review ☐

	Performed By		
	Initials	Date	N/A
1. Submit financial statements and report to typing.	______	______	☐
2. Proofread the financial statements and report.	______	______	☐
3. Resubmit the financial statements and report for correction.	______	______	☐
4. Submit to technical reviewer, if applicable.	______	______	☐
5. Resubmit the financial statements and report for corrections.	______	______	☐
6. Foot and crossfoot all pages.	______	______	☐
7. Submit to engagement partner for final review.	______	______	☐
8. Release the financial statements and report.	______	______	

Number of Copies:

Bound: ______ Unbound: ______

11.700 SAMPLE REPORTS FOR PERSONAL FINANCIAL STATEMENT ENGAGEMENTS

11.701 The following pages include illustrative reports for various engagements involving personal financial statements.

11.702 The illustrative reports in this chapter are included in the WordPerfect diskette provided with the Manual.

Sample Reports — PFS

SAMPLE REPORTS FOR PERSONAL FINANCIAL STATEMENT ENGAGEMENTS

SAMPLE REPORTS FOR PERSONAL FINANCIAL STATEMENT ENGAGEMENTS (CONTINUED)

11.703 Standard Compilation Report — Statement of Financial Condition Only

____
____
____

I (We) have compiled the accompanying statement of financial condition of __________________ [client's name] as of ____________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying statement of financial condition and, accordingly, do not express an opinion or any other form of assurance on it.

[Signature]

[Date]

11.704 Standard Compilation Report — Statement of Financial Condition and Statement of Changes in Net Worth

____

____

____

I (We) have compiled the accompanying statement of financial condition of ________________ [client's name] as of __________________ [financial statement date], and the related statement of changes in net worth for the __________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

11.705 Compilation Report — Lack of Independence

____
____
____

I (We) have compiled the accompanying statement of financial condition of __________________ [client's name] as of __________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying statement of financial condition and, accordingly, do not express an opinion or any other form of assurance on it.

I am (We are) not independent with respect to __________________ [client's name].

[Signature]

[Date]

11.706 Compilation Report — Substantially All Disclosures Omitted

____
____
____

I (We) have compiled the accompanying statement of financial condition of ____________________ [client's name] as of ______________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. (The statement of financial condition is intended to present the assets of ______________________ [client's name] at estimated current values and their liabilities at estimated current amounts.)[1]

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying statement of financial condition and, accordingly, do not express an opinion or any other form of assurance on it.

__________________ [client's name] have elected to omit substantially all of the disclosures required by generally accepted accounting principles. If the omitted disclosures were included in the financial statement, they might influence the user's conclusions about the financial condition of ____________________ [client's name]. Accordingly, this financial statement is not designed for those who are not informed about such matters.

[Signature]

[Date]

Note:

[1] This statement should be included if the financial statement does not disclose the basis of accounting.

11.707 Compilation Report — Departure from GAAP — Material Assets Valued at Cost

____
____
____

I (We) have compiled the accompanying statement of financial condition of ____________________ [client's name] as of ____________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying statement of financial condition and, accordingly, do not express an opinion or any other form of assurance on it. However, I (we) did become aware of a departure from generally accepted accounting principles that is described in the following paragraph.

As disclosed in Note ___ to the financial statement, generally accepted accounting principles require that assets be presented at their estimated current values and that liabilities be presented at their estimated current amounts. ________________ [client's name] have informed me (us) that their investment in ________________ [investee's name] is stated in the accompanying financial statement at cost and that the effects of this departure from generally accepted accounting principles have not been determined.

[Signature]

[Date]

11.708 Compilation Report—Departure from GAAP—Failure to Include Estimated Income Taxes

____

____

____

I (We) have compiled the accompanying statement of financial condition of ____________________ [client's name] as of ____________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying statement of financial condition and, accordingly, do not express an opinion or any other form of assurance on it. However, I (we) did become aware of a departure from generally accepted accounting principles that is described in the following paragraph.

Generally accepted accounting principles require that personal financial statements include a provision for estimated income taxes on the differences between the estimated current values of assets and the estimated current amounts of liabilities and their tax bases. The accompanying statement of financial condition does not include such a provision, and the effect of this departure from generally accepted accounting principles has not been determined.

[Signature]

[Date]

11.709 Compilation Report — Personal Financial Statement With Accompanying Supplementary Information

____
____
____

I (We) have compiled the accompanying statement of financial condition of ____________________ [client's name] as of ________________ [financial statement date], and the accompanying supplementary information contained in ______________________ [identify schedules], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying statement of financial condition and supplementary information and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

11.710 Compilation Report — Personal Financial Statement Included in a Prescribed Form

____
____
____

I (We) have compiled the accompanying statement of financial condition of ________________ [client's name] as of _______________ [financial statement date], included in the accompanying prescribed form, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

My (Our) compilation was limited to presenting in the form prescribed by __________________ [identify the body] information that is the representation of the individuals whose financial statement is presented. I (We) have not audited or reviewed the financial statement referred to above and, accordingly, do not express an opinion or any other form of assurance on it.

This financial statement (and the related disclosures) is (are) presented in accordance with the requirements of _______________________ [identify the body], which differ from generally accepted accounting principles. Accordingly, this financial statement is not designed for those who are not informed about such differences.

[Signature]

[Date]

11.711 Compilation Report — Income Tax Basis

____
____
____

I (We) have compiled the accompanying statement of assets and liabilities — income tax basis of ________________ [client's name] as of _______________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying statement and, accordingly, do not express an opinion or any other form of assurance on it.

[Signature]

[Date]

11.712 Compilation Report — Historical Cost Basis

____
____
____

I (We) have compiled the accompanying statement of assets and liabilities — historical cost basis of __________________ [client's name] as of _______________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying financial statement and, accordingly, do not express an opinion or any other form of assurance on it.

[Signature]

[Date]

11.713 Compilation Report — Statement of Financial Condition With Supplementary Historical Cost Information

____
____
____

I (We) have compiled the accompanying statement of financial condition and accompanying supplementary historical cost information of ____________________ [client's name] as of ____________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of the individuals whose financial statements are presented. I (We) have not audited or reviewed the accompanying statement of financial condition and supplementary historical cost information and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

11.714 Report on Personal Financial Statement Included With a Personal Financial Plan

____
____
____

The accompanying statement of financial condition of _______________ [client's name], as of __________________ [financial statement date], was prepared solely to help you develop your personal financial plan. Accordingly, it may be incomplete or contain other departures from generally accepted accounting principles and should not be used to obtain credit or for any purposes other than developing your financial plan. I (We) have not audited, reviewed, or compiled the statement.

[Signature]

[Date]

11.715 Standard Review Report — Statement of Financial Condition Only

____
____
____

I (We) have reviewed the accompanying statement of financial condition of ____________________ [client's name] as of ____________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this financial statement is the representation of ______________ [client's name].

A review of personal financial statements consists principally of inquiries of the individuals whose financial statements are presented and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying statement of financial condition in order for it to be in conformity with generally accepted accounting principles.

[Signature]

[Date]

11.716 Standard Review Report — Statement of Financial Condition and Statement of Changes In Net Worth

____
____
____

I (We) have reviewed the accompanying statement of financial condition of ________________ [client's name] as of __________________ [financial statement date], and the related statement of changes in net worth for the ____________ [period] then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of __________ [client's name].

A review of personal financial statements consists principally of inquiries of the individuals whose financial statements are presented and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

[Signature]

[Date]

11.717 Review Report — GAAP Departure — Failure to Include Estimated Income Taxes

____
____
____

I (We) have reviewed the accompanying statement of financial condition of __________________ [client's name] as of ____________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this financial statement is the representation of ______________ [client's name].

A review of personal financial statements consists principally of inquiries of the individuals whose financial statements are presented and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, with the exception of the matter described in the following paragraph, I am (we are) not aware of any material modifications that should be made to the accompanying statement of financial condition in order for it to be in conformity with generally accepted accounting principles.

Generally accepted accounting principles require that personal financial statements include a provision for estimated income taxes on the differences between the estimated current values of assets and the estimated current amounts of liabilities and their tax bases. The accompanying statement of financial condition does not include such a provision and the effect of this departure from generally accepted accounting principles has not been determined.

[Signature]

[Date]

11.718 Review Report — Financial Statement With Accompanying Reviewed Supplementary Information

____

____

____

I (We) have reviewed the accompanying statement of financial condition of __________________ [client's name] as of ___________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this financial statement is the representation of _____________ [client's name].

A review of personal financial statements consists principally of inquiries of the individuals whose financial statements are presented and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statement in order for it to be in conformity with generally accepted accounting principles.

The information in ___________________ [identify schedules] accompanying the financial statement is presented only for supplementary analysis purposes and has been subjected to the inquiry and analytical procedures applied in the review of the basic financial statement. I (We) did not become aware of any material modifications that should be made to such information.

[Signature]

[Date]

11.719 Review Report — Financial Statement With Accompanying Compiled Supplementary Information

____
____
____

I (We) have reviewed the accompanying statement of financial condition of ________________ [client's name] as of ________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this financial statement is the representation of ____________ [client's name].

A review of personal financial statements consists principally of inquiries of the individuals whose financial statements are presented and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statement in order for it to be in conformity with generally accepted accounting principles.

The information in ________________ [identify schedules] accompanying the financial statement is presented only for supplementary analysis purposes and has not been subjected to the inquiry and analytical procedures applied in the review of the basic financial statement, but was compiled, without audit or review, from information that is the representation of ________________ [client's name]. I (We) do not express an opinion or any other form of assurance on such information.

[Signature]

[Date]

11.720 Review Report — Income Tax Basis

____
____
____

I (We) have reviewed the accompanying statement of assets and liabilities — income tax basis of ____________________ [client's name] as of ____________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this financial statement is the representation of ____________________ [client's name].

A review of personal financial statements consists principally of inquiries of the individuals whose financial statements are presented and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statement in order for it to be in conformity with the income tax basis of accounting described in Note ____.

[Signature]

[Date]

11.721 Review Report — Historical Cost Basis

____

____

____

I (We) have reviewed the accompanying statement of assets and liabilities — historical cost basis of __________________ [client's name] as of _________________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this financial statement is the representation of __________________ [client's name].

A review of personal financial statements consists principally of inquiries of the individuals whose financial statements are presented and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statement in order for it to be in conformity with the historical cost basis of accounting described in Note ___.

[Signature]

[Date]

Special Report Engagements

CHAPTER 12

SPECIAL REPORTS

Table of Contents

CHAPTER 12

SPECIAL REPORTS

Table of Contents (Continued)

CHAPTER 12

SPECIAL REPORTS

12.000 INTRODUCTION

12.001 Accountants may be engaged to report on various special-purpose financial presentations of nonpublic entities that do not meet the definition of generally accepted accounting principles (GAAP) or other comprehensive bases of accounting (OCBOA) financial statements. For example, an entity may engage an accountant to compile or review a separate presentation of a specified element, account, or item of a financial statement or to compile or review a financial statement prepared under a contractual or regulatory basis of accounting. In addition, accountants may provide compilation or review services to entities with special circumstances, such as development stage companies and companies reporting on less than or more than a 12-month period. This chapter provides guidance on these special reporting situations.

12.002 The AICPA's Accounting and Review Services Committee is authorized to establish standards for both the unaudited financial statements and *other unaudited financial information* of nonpublic entities. The committee, however, has confined its pronouncements primarily to financial statements. Therefore, some of the guidance for unaudited financial information has to be inferred from similar guidance for audited financial statements. In addition, the committee has not addressed reporting guidance for most special-circumstance entities. This guidance must be extrapolated from similar guidance in other professional literature, such as the auditing literature.

12.100 REPORTING ON SPECIFIED ELEMENTS, ACCOUNTS, OR ITEMS OF A FINANCIAL STATEMENT

12.101 An accountant may be asked to report on a separate presentation of specified elements, accounts, or items of a financial statement. Examples of such information include a schedule of net sales, a schedule of inventories, a schedule of accounts receivable, and a schedule of general and administrative expenses. The initial question the accountant must address is what types of accounting services are appropriate for this type of information.

12.102 Professional literature recognizes three specific services that an accountant may provide for specified elements, accounts, or items of a financial statement: (1) audits, (2) reviews, and (3) agreed-upon procedures. The authors believe that a fourth service, compilation, is also appropriate, although professional literature is silent about such a service. Each of these four services is discussed below. These services pertain to *separate* presentations of elements, accounts, or items. If such information is presented along with the financial statements as supplementary information, the accountant should follow the guidance in Chapters 5 and 7 concerning compilation and review of supplementary information.

Audits of Specified Elements, Accounts, or Items of a Financial Statement

12.103 Statements on Auditing Standards (SAS) No. 62, *Special Reports,* permits an accountant to audit specified elements, accounts, or items and provides guidance about reporting when an audit has been conducted. The accountant should refer to SAS No. 62 if he or she is engaged to audit specified elements, accounts, or items.

Reviews of Specified Elements, Accounts, or Items of a Financial Statement

12.104 An accountant may accept an engagement to review specified elements, accounts, or items. However, such a review is governed by the Attestation Standards, *not* by Statements on Standards for Accounting and Review Services (SSARS). SSARS No. 1, Interpretation No. 8, *Reports on Specified Elements, Accounts, or Items of a Financial Statement* (AR 9100.27-.28), states that SSARS provides guidance concerning the unaudited *financial statements* of nonpublic entities and, because an element, account, or item is not a financial statement, SSARS does not apply to them. The Interpretation goes on to state that an accountant may review an element, account, or item under the attestation standards. The accountant should refer to the Attestation Standards if he or she is engaged to review specified elements, accounts, or items. (See section 12.402 for an illustration of a review report on specified elements, accounts, or items of a financial statement based on the Attestation Standards.)

Agreed-Upon Procedures Applied to Specified Elements, Accounts, or Items of a Financial Statement

12.105 SAS No. 75, *Engagements to Apply Agreed-Upon Procedures to Specified Elements, Accounts, or Items of a Financial Statement*, which is being issued as this edition goes to print, supersedes SAS No. 35 of a similar name. Like SAS No. 35, SAS No. 75 permits an accountant to apply agreed-upon procedures to elements, accounts, or items of a financial statement and issue a report. The accountant should refer to SAS No. 75 if he or she is engaged to apply agreed-upon procedures to such information.

Compilations of Elements, Accounts, or Items of a Financial Statement

12.106 SSARS No. 1 provides guidance for the compilation and review of complete financial statements; not for specified elements, accounts, or items of a financial statement. Therefore, the accountant is not required to report on specified elements, accounts, or items, even when the accountant prepares and submits such presentations to a client or a third party. That is, the presentation of specified elements, accounts, or items of a financial statement may be conveyed (1) without any report, (2) with a simple transmittal letter, or (3) with a report that is descriptive of the accountant's services.

12.107 If the accountant decides to follow alternative three in section 12.106 and issue a report on the compilation of specified elements, accounts, or items of a financial statement, the authors suggest that the accountant comply with the performance standards contained in SSARS, and model the report after the compilation report on financial statements contained in SSARS No. 1. However, the reference to SSARS should be omitted. (See section 12.403 for an illustration of a compilation report on specified elements, accounts, or items of a financial statement.)

12.200 SPECIAL-PURPOSE FINANCIAL PRESENTATIONS TO COMPLY WITH CONTRACTUAL AGREEMENTS OR REGULATORY PROVISIONS

12.201 Occasionally clients are asked to prepare a special-purpose presentation that complies with the requirements of a contractual agreement or regulatory provision. The contractual agreement or regulatory provision may require a financial presentation that —

1. Does not constitute a complete presentation of the entity's assets, liabilities, revenues, or expenses, but is otherwise prepared in conformity with GAAP or OCBOA, or

2. Is based on a prescribed method of accounting that does not result in a presentation in conformity with GAAP or OCBOA.

12.202 SSARS No. 1, Interpretation No. 18, *Special-Purpose Financial Presentations to Comply With Contractual Agreements or Regulatory Provisions* (AR 9100.63–.72), states that an accountant may compile or review these types of presentations, and provides guidance on the content of the accountant's report. This guidance is discussed as follows.

Incomplete Presentation That Is Otherwise in Conformity with GAAP or OCBOA

12.203 A contractual agreement or regulatory provision may require a financial statement that does not constitute a complete presentation of the entity's assets, liabilities, revenues or expenses, but is otherwise prepared in conformity with GAAP or OCBOA. For example, a purchase agreement may require an entity to provide a schedule of net assets sold, measured in conformity with GAAP, but limited to the asset to be sold and liabilities to be transferred. Another example is a loan agreement that requires a statement of revenues and expenses that is otherwise prepared in accordance with GAAP, but omits interest, depreciation, and amortization expense. These special-purpose financial presentations should generally be considered as financial statements because they contain too many items to constitute elements, accounts, or items of a financial statement.

12.204 Interpretation No. 18 of SSARS No. 1 establishes presentation requirements for compiled or reviewed incomplete presentations. Such presentations should —

- Include the disclosure of the basis of presentation in the notes to the financial statements
- Differ from financial statements prepared in accordance with GAAP or OCBOA only to the extent necessary to meet the special purpose for which the presentation is prepared
- Contain similar informative disclosures when the presentation contains items that are the same as, or similar to, those contained in a full set of financial statements
- Include titles that avoid any implication that the special-purpose financial statements are intended to present financial position, results of operations, or cash flows

12.205 Interpretation No. 18 also establishes reporting guidance for accountants who compile or review incomplete special-purpose financial statements. The Interpretation requires that the accountant's compilation or review report on such presentations be expanded to include two explanatory paragraphs that contain the following information:

First Additional Paragraph

- An explanation of what the presentation is intended to present and a reference to a note to the financial statements that describes the basis of accounting. In a compilation engagement in which the entity chooses to omit substantially all of the disclosures and does not disclose the basis of presentation, the accountant should disclose the basis in the compilation report.
- If the presentation is an OCBOA presentation, state that the basis of presentation is a comprehensive basis of accounting other than GAAP.
- An indication that the presentation is not intended to be a complete presentation of the entity's assets, liabilities, revenues, and expenses.

Second Additional Paragraph

- A statement that the distribution of the report is restricted to those within the entity, to parties to the contract or agreement, for filing with a regulatory agency, or to those with whom the entity is negotiating directly. (Certain reports filed with regulatory agencies are a matter of public record. In those circumstances, the report should state that the restriction is not intended to limit the distribution of the report, which is a matter of public record.)

See sections 12.404 and 12.406 for illustrative compilation and review reports on incomplete presentations.

Presentation Prescribed in a Contractual Agreement That Is Not in Conformity with GAAP or OCBOA

12.206 The second type of special-purpose presentation is one that is prepared in conformity with a basis of accounting prescribed in a contractual agreement that results in a presentation that is not in conformity with GAAP or OCBOA. For example, an acquisition agreement may require an entity to prepare financial statements in which certain assets, such as inventories and properties, are presented in conformity with a valuation basis that is neither GAAP nor OCBOA. Another example is a loan agreement that requires the borrower to prepare financial statements in which inventories are presented based on their net realizable value.

12.207 Interpretation No. 18 states that special-purpose presentations prepared in conformity with a basis of accounting that is not GAAP or OCBOA should—

- Include disclosure of the basis of presentation in the notes to the financial statements.
- Contain similar informative disclosures when the presentation contains items that are the same as, or similar to, those contained in GAAP or OCBOA financial statements.

- Include titles that avoid any implication that the special-purpose financial statements are intended to present financial position, results of operations, or cash flows.

12.208 Interpretation No. 18 also establishes reporting guidance for accountants who compile or review special-purpose financial presentations that are not in conformity with GAAP or OCBOA. The Interpretation requires that the accountant's compilation or review report on such presentations be expanded to include two explanatory paragraphs that contain the following information:

First Additional Paragraph

- An explanation of what the presentation is intended to present, a reference to a note to the financial statements that describes the basis of presentation, and an explanation that the presentation is not intended to be a presentation in conformity with generally accepted accounting principles. In a compilation engagement in which the entity chooses to omit substantially all of the disclosures and does not disclose in the financial statements the basis of presentation, the accountant should disclose the basis in the compilation report.
- A description of any significant interpretations made by management of the contractual agreement.

Second Additional Paragraph

- A statement that the distribution of the report is restricted to those within the entity, to parties to the contract or agreement, or to those with whom the entity is negotiating directly.

12.209 In a review engagement, one additional report modification is necessary. The standard review report includes a statement that the accountant is not aware of any material modifications that should be made to the financial statements for them to be in conformity with GAAP. Therefore, if the special-purpose presentation is not intended to be in conformity with GAAP, the accountant should modify the standard review report to refer to the basis of accounting prescribed by the contractual agreement.

12.210 In either a compilation or review engagement, if the accountant becomes aware of material departures from the basis of presentation described, the accountant should consider whether modification of his or her report is adequate to disclose such a departure. (See sections 12.405 and 12.407 for illustrative compilation and review reports on special-purpose presentations not intended to be in conformity with GAAP or OCBOA.)

12.300 REPORTS ON ENTITIES WITH SPECIAL CIRCUMSTANCES

12.301 Accountants who have been engaged to compile or review an entity's financial statements sometimes encounter special circumstances that affect the language in the accountant's report. This section discusses several common situations and suggests reporting approaches for them.

Financial Statements Covering a Period Shorter Than or Longer Than 12 Months

12.302 Compilation or review reports as of the end of an entity's first year of operations often cover less than 12 months. That is, the period from the start of operations to the fiscal year end is less than 12 months. In such situations, the first paragraph of the standard compilation or review report should be modified to refer to the period covered by the financial statements—the date operations commenced to the end of the fiscal year. (See section 12.408 for an illustration of a compilation report on the first year of operations.)

12.303 Occasionally accountants may be engaged to report on financial statements that cover a period longer than 12 months. For example, the accountant's first engagement for a client may involve reporting on financial statements covering a period in excess of 12 months. AICPA Technical Practice Aid (TPA 9900.07) indicates that such reports are appropriate as long as the title of the financial statements and the accountant's report clearly indicate the period covered by the financial statements.

Development Stage Enterprises

12.304 Generally accepted accounting principles require enterprises in the development stage to present certain additional information in their financial statements. This additional information ordinarily involves cumulative revenue and expenses from the entity's inception and cumulative sources and uses of financial resources from inception.

12.305 Because this additional information is required by GAAP, it is considered to be a part of the basic financial statements, not supplementary information. Therefore, the first paragraph of the accountant's compilation or review report should be modified to (a) identify the entity as being in the development stage and (b) report on the cumulative information required by GAAP. (See section 12.409 for an illustration of a compilation report for a development stage company, and section 13.500 of Chapter 13 for a description of the presentation guidelines for financial statements of a development stage company.)

Sample Reports —
Special-Purpose

12.400 SAMPLE REPORTS

12.401 The illustrative reports in this chapter contain the SSARS No. 7 wording.

12.402 Review Report on Elements, Accounts, or Items of a Financial Statement Under the Attestation Standards

____
____
____

I (We) have reviewed the accompanying ______________ [identify the schedule(s) of elements, accounts, or items] of ____________ [client name] for the ______ [period] ended __________. My (Our) review was conducted in accordance with standards established by the American Institute of Certified Public Accountants.

A review is substantially less in scope than an examination, the objective of which is the expression of an opinion on the ___________________ [identify the schedule(s) of elements, accounts or items]. Accordingly, I (we) do not express such an opinion.[1]

Based on my (our) review, nothing came to my (our) attention that caused me (us) to believe that the accompanying ________________ [identify the schedule(s) of elements, accounts or items] is (are) not presented in conformity with generally accepted accounting principles (or other identified basis of accounting).

[Signature]

[Date]

Note:

[1] An additional explanatory paragraph may be added after the second paragraph to emphasize matters relating to the presentation of the element or the review engagement.

12.403 Compilation Report on Specified Elements, Accounts, or Items of a Financial Statement

____
____
____

I (We) have compiled the accompanying ______________ [identify the schedule(s) of elements, accounts, or items] of ________________________ [client name] for the __________ [period] ended ________________.

My (Our) compilation was limited to presenting in the form of a ______________ [identify the schedule(s) of elements, accounts or items] information that is the representation of management (the owners). I (We) have not audited or reviewed the accompanying ______________ [identify the schedule(s) of elements, accounts or items] and, accordingly, do not express an opinion or any other form of assurance on it (them).

[Signature]

[Date]

12.404 Compilation Report on Special-Purpose Financial Presentation That Is an Incomplete Presentation Prepared in Accordance with an Acquisition Agreement But Is Otherwise in Conformity with GAAP or OCBOA

____
____
____

I (We) have compiled the accompanying statement of net assets sold of __________________________ [company name] as of _________________ [financial statement date] in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying statement and, accordingly do not express an opinion or any form of assurance on it.

The accompanying statement was prepared to present the net assets of __________________________ [company name] sold to _______________________________ [purchasing company] pursuant to the purchase agreement described in Note ______, and is not intended to be a complete presentation of ______________________ [company's] assets and liabilities.

This report is intended solely for the information and use of the boards of directors and managements of ________________________ [company name] and ______________________ [purchasing company] and should not be used for any other purpose.

[Signature]

[Date]

12.405 Compilation Report on Special-Purpose Financial Presentation Pursuant to an Acquisition Agreement That Results in a Presentation That Is Not in Conformity with GAAP or OCBOA

____
____
____

I (We) have compiled the special-purpose statement of assets and liabilities of ____________________ [company name] as of _______________ [financial statement date] and the related special-purpose statements of revenues and expenses and of cash flows for the year then ended in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying special-purpose financial statements and, accordingly, do not express an opinion or any form of assurance on them.

The accompanying special-purpose financial statements were prepared for the purpose of complying with the acquisition agreement between ______________________________ [company name] and _____________________ [purchasing company] described in Note _____, and are not intended to be a presentation in conformity with generally accepted accounting principles.

This report is intended for the information and use of the boards of directors and managements of _____________________ [company name] and __________________ [purchasing company] and should not be used for any other purpose.

[Signature]

[Date]

12.406 Review Report on Special-Purpose Financial Presentation That Is an Incomplete Presentation Prepared in Accordance With an Acquisition Agreement But Is Otherwise in Conformity with GAAP or OCBOA

____

____

____

I (We) have reviewed the accompanying statement of net assets sold of ______________________ [company name] as of __________________ [financial statement date] in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this statement is the representation of management (the owners) of ____________________ [company name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion on the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

The accompanying statement was prepared to present the net assets of ____________________ [company name] sold to __________________________ [purchasing company] pursuant to the purchase agreement described in Note _____, and is not intended to be a complete presentation of ___________________ [company's] assets and liabilities.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying statement of net assets sold in order for it to be in conformity with generally accepted accounting principles.

This report is intended solely for the information and use of the boards of directors and managements of ____________________ [company name] and ____________________ [purchasing company] and should not be used for any other purpose.

[Signature]

[Date]

12.407 Review Report on Special-Purpose Financial Presentation Pursuant to an Acquisition Agreement That Results in a Presentation That Is Not in Conformity with GAAP or OCBOA

____
____
____

I (We) have reviewed the special-purpose statement of assets and liabilities of ____________________ [company name] as of __________________ [financial statement date] and the related special-purpose statements of revenues and expenses and of cash flows for the year then ended in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of management (the owners) of ______________________ [company name].

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion on the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

The accompanying special-purpose financial statements were prepared for the purpose of complying with the acquisition agreement between __________________ [company name] and __________________ [purchasing company] described in Note ______, and are not intended to be a presentation in conformity with generally accepted accounting principles.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying special-purpose financial statements in order for them to be in conformity with the basis of accounting described in Note ______.

This report is intended for the information and use of the boards of directors and managements of ______________________ [company name] and ____________________ [purchasing company] and should not be used for any other purpose.

[Signature]

[Date]

12.408 Compilation Report — Entity's First Year of Operations and Financial Statements Covering a Period of Less Than 12 Months

____

____

____

I (We) have compiled the accompanying balance sheets of ______________________________ [client name] as of _______________ [financial statement date], and the related statements of income, changes in shareholders' equity, and cash flows for the period from beginning of operations _____________ [date operations began] (Inception) to _______________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

12.409 Compilation Report — Development Stage Enterprise

____
____
____

I (We) have compiled the accompanying balance sheets of ________________________________ [client name] (a development stage enterprise) as of ______________ [financial statement date], and the related statements of operations, shareholders' equity, and cash flows for the year then ended and for the period from beginning of operations ___________ [date operations began] (inception) to ____________ [financial statement date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

[Signature]

[Date]

Prospective
Financial Information

CHAPTER 13

PROSPECTIVE FINANCIAL INFORMATION

Table of Contents

Table of Contents (Continued)

CHAPTER 13

PROSPECTIVE FINANCIAL INFORMATION

Table of Contents (Continued)

CHAPTER 13

PROSPECTIVE FINANCIAL INFORMATION

13.000 INTRODUCTION

13.001 Practitioners increasingly are being asked to provide services that involve prospective financial information. For example, many accountants assist clients in preparing cash budgets to help in the financial management of their businesses. Accountants also prepare tax projections to assist their clients in tax planning. In addition, prospective financial statements are a required part of the documentation for many loans, including those administered by the Small Business Administration.

Authoritative Standards for Prospective Financial Information

13.002 There are several authoritative documents issued by the AICPA that apply to prospective financial statements, including:

- *Guide for Prospective Financial Information* (the Guide) (Product No. 011140), which was updated in 1995 to incorporate Statements of Position (SOPs) 89-3, *Questions Concerning Accountants' Services on Prospective Financial Statements;* 90-1, *Accountants' Services on Prospective Financial Statements for Internal Use Only and Partial Presentations;* and 92-2, *Questions and Answers on the Term* Reasonably Objective Basis and *Other Issues Affecting Prospective Financial Statements.*
- Codification of Statements on Standards for Attestation Engagements (SSAE), *Attestation Standards,* (Section 200) (Product No. 057265).
- Statement on Standards for Attestation Engagements No. 4, *Agreed-Upon Procedures Engagements,* was issued in September 1995 and is effective for reports on agreed-upon procedures engagements dated after April 30, 1996. Earlier application is encouraged.

SSAE No. 4 supersedes and amends certain paragraphs in SSAE No. 1, Section 200, "*Financial Forecast and Projections*", as noted later in this chapter.

SOP 90-1 and the *Guide for Prospective Financial Information* will also be revised to conform with the provisions of SSAE No. 4.

Practice Tip:

Because SSARS No. 1 specifically states that the compilation and review standards do not apply to financial forecasts, projections and similar presentations, accountants should look to the literature listed above for guidance when performing such services.

Definitions

13.003 To understand the guidance related to prospective financial statements, it is important to understand the definition of the following terms:

Prospective financial information — Encompasses all types of prospective data presented whether in the form of a financial statement or in any other form, such as a partial presentation or a tax projection.

Prospective financial statements — Information that presents financial position, results of operations, and cash flows for one or more future periods. Prospective financial statements are either forecasts or projections.

Responsible party — The person or persons who are responsible for the assumptions underlying the prospective financial information. Usually, the responsible party is management of the entity.

Financial forecast — Prospective financial information that presents, to the best of the responsible party's knowledge and belief, expected financial position, results of operations, and cash flows. Only a financial forecast is appropriate for general use. "General use" refers to the use of the statements by persons with whom the responsible party is not negotiating directly.

Key factors — The significant matters on which an entity's future results are expected to depend, such as the level of sales and production and financing activities. These factors are basic to the entity's operations and serve as a foundation for prospective financial statements and are the bases for the underlying assumptions.

Financial projection — Prospective financial information that presents, to the best of the responsible party's knowledge and belief, given one or more hypothetical assumptions, expected financial position, results of operations and cash flows. A financial projection is only appropriate for limited use by management or third parties with whom management is negotiating directly. For example, a bank with whom management is negotiating for a loan.

Hypothetical assumption — An assumption used in a financial projection to present a condition or course of action that is not necessarily expected to occur, but is consistent with the purpose of the projection. A hypothetical assumption presents a "what if" scenario. Although the hypothetical assumption is not expected to occur, it should be consistent with the purpose of the projection.

Complete presentation — Usually, a balance sheet, a statement of income, and a statement of cash flows, but at least the following minimum financial statement elements:

a. Sales or gross revenues

b. Gross profit or cost of sales

c. Unusual or infrequently occurring items

d. Provision for income taxes

e. Income from continuing operations

f. Discontinued operations or extraordinary items

g. Net income

h. Primary and fully diluted earnings per share (for public companies)

i. Significant changes in financial position

Required Disclosures

j. A description of what the responsible party intends the prospective financial information to present, a statement that the assumptions are based upon the responsible party's judgment at the time the prospective information was prepared, and a caveat that the prospective results may not be attained.

k. Summary of significant assumptions

l. Summary of significant accounting policies

Partial presentation — Presentations that omit one or more of the applicable minimum items (a through i) required for a complete presentation. Items j through l (above) are disclosures that should accompany the prospective financial information whether the presentation is limited to applicable minimum items or presents more detail.

> **Practice Tip:**
>
> The omission of items j, k, or l from a presentation that contains at least the applicable minimum items would not make it a partial presentation; it would be a deficient presentation because of the lack of required disclosures.

Feasibility study — An analysis of a proposed course of action, such as an investment. A feasibility study may involve the preparation of prospective financial information. Alternatively, prospective financial information may be prepared based on the results of a feasibility study.

Budgets — A quantitative expression of a plan of action. Since budgets may represent expected results or some ideal level of performance, they may or may not be equivalent to a financial forecast.

Pro forma financial information — Illustrates what an entity's historical financial information might have been had an event or transaction occurred at an earlier date. A pro forma presentation is restated historical financial information; it is not prospective financial information.

13.100 TYPES OF PROFESSIONAL SERVICES

13.101 The type of service that is appropriate for prospective financial information depends on the use and the nature of the information. Prospective financial statements may be prepared for internal use only or for third parties, and the presentations may be complete or partial. The authoritative standards provide for a number of different services related to prospective financial statements, as summarized below:

Presentations for third parties:

- Examination
- Agreed-upon procedures
- Compilation
- Special disclaimer on budgets

Presentations for internal use only:

- Plain paper
- Assembly

Practice Tip:

The original guidance for accountant's services on prospective financial statements included a review as the highest level of service rather than an examination. This was changed with the issuance of the Statement on Standards for Accountants' Services on Prospective Financial Information in 1985. That standard established an examination as the highest level of service, and it prohibits reviews of prospective financial statements.

Presentations for Third Parties

13.102 Examination Service. An examination service is the highest level of service an accountant can provide on prospective financial information. This service includes performing the following general procedures:

1. Evaluating the preparation of the financial forecast or projection.

2. Evaluating the support for the underlying assumptions.

3. Evaluating the presentation of the financial forecast or projection for conformity with AICPA presentation guidelines.

4. Issuing an examination report.

13.103 Agreed-Upon Procedures. Agreed-upon procedures may be applied to prospective financial information provided:

1. The specified user has participated in establishing the nature and scope of the engagement and takes responsibility for the adequacy of the accountant's procedures.

2. Distribution of the report is restricted to the specified users.

3. The prospective financial information includes a summary of the significant assumptions.

As this edition of the Manual went to print, the Auditing Standards Board (ASB) is expected to soon issue SSAE No. 4, *Agreed-Upon Procedures Engagements,* which is effective for reports on agreed-upon procedures engagements dated after April 30, 1996. SSAE No. 4 sets forth the following additional requirements:

4. Criteria (accounting principles, policies, and assumptions), including materiality limits, to be used in the determination of findings must be agreed upon between the accountant and the specified users.

5. The procedures to be applied to the prospective financial statements must be expected to result in findings that are capable of reasonably consistent estimation or measurement using the criteria.

6. Evidential matter related to the prospective financial statements to which the procedures are applied must be expected to exist to provide a reasonable basis for expressing the findings in the accountant's report.

SSAE No. 4 restates and emphasizes the requirements that the accountant and the specified users agree upon the procedures to be performed, and that the specified users take responsibility for the sufficiency of the agreed-upon procedures for their purposes.

SSAE No. 4 is also discussed in Chapter 1, sections 1.631-1.639. Although the new standard is not yet effective, many of the concepts can be applied currently. Practitioners should be alert to ensure that they comply as the new standard becomes effective.

13.104 Compilation Service. A compilation service is the lowest level of service an accountant can perform on prospective financial statements intended for use by third parties. A compilation involves:

1. Assembling, to the extent necessary, the prospective information based on the responsible party's (usually management's) assumptions,

2. Performing certain compilation procedures,

3. Considering whether the presentation guidelines in the Guide have been followed, and

4. Issuing a compilation report.

Presentations for Internal Use Only

13.105 When the prospective financial statements are to be restricted to internal use only, an accountant may perform a compilation, examination, or agreed-upon procedures. However, the accountant may also perform a spectrum of other services on the statements. In determining whether prospective financial statements will be restricted to internal use, the accountant may rely on the written or oral representations of the responsible party, unless the accountant becomes aware of information that contradicts the responsible party's representations.

13.106 Plain Paper Service. An accountant may provide services on prospective financial statements for internal use only and submit them to the client on plain paper. In performing a plain paper service, the accountant performs one or more procedures on the prospective financial statements but does not report on them. Obviously, the accountant's name should not be associated with the presentation. This is the only situation in which it is not required for the assumptions to be presented.

Practice Tip:

While the accountant may omit the significant assumptions in plain paper engagements, it is recommended that the assumptions be presented even in these situations. However, the assumptions may be presented in an informal manner, such as the output from a computer spreadsheet.

Practice Tip:

A plain paper presentation should not be accompanied by the accountant's report or transmittal letter, bound in the accountant's report cover, printed on paper containing the accountant's logo or watermark, or bound with historical financial statements that were audited, reviewed, or compiled by the accountant.

13.107 Assembly Service. An assembly service includes the manual or computer processing of the clerical functions required to prepare prospective financial information. Assembly services are similar to plain paper services, except that the accountant issues a report on the work performed. In performing an assembly service, the accountant considers whether the client has identified all key factors affecting the prospective financial information and developed assumptions about all these factors. Then the accountant translates the assumptions into the prospective information. These procedures are significantly less than those required to compile prospective financial statements. However, because the accountant is reporting on the prospective financial statements, the presentation must include the significant assumptions.

13.108 Special Disclaimer for Budget Presented With Interim Information. If a financial forecast is presented in an accountant-submitted document that also contains the accountant's compilation, review, or audit report on the entity's historical financial statements, the accountant is required to compile, examine, or apply agreed-upon procedures to the forecast unless it: (1) is labeled as a "budget," (2) does not extend beyond the end of the current fiscal year, and (3) is presented with interim historical financial statements for the current year. In such circumstances, the accountant does not have to compile, examine, or apply agreed-upon procedures to the budget. However, the accountant must report on the budget and (a) indicate that he or she did not perform any procedures on the budget, and (b) disclaim an opinion on the budget.

Determining the Appropriate Type of Service

13.109 The major consideration in determining the appropriate type of service to provide to a client is whether the prospective financial information is for internal use only. Prospective financial information to be used only by the responsible party and others within the entity are considered internal-use-only prospective financial information. Any form of prospective financial information, including forecasts, projections, and partial presentations, may be appropriate for internal use only. When the accountant provides services in connection with prospective financial statements for internal use only or partial presentations, he or she may present the information on plain paper or with an assembly report. Of course, the accountant may also provide a higher level of service, such as a compilation, examination, or agreed-upon procedures.

13.110 When the accountant submits to his or her client or others a financial forecast or projection for use by a third party, the accountant should examine, compile, or apply agreed-upon procedures to the presentation. However, there is the special exemption for a budget presented with interim financial statements, as described above.

13.111 Prospective financial information that is for third party use may be designed for general use or limited use. **General use** refers to the use of the information by a party with whom the responsible party is not negotiating directly. Because these parties are unable to ask the responsible party about the presentation, the appropriate presentation is one that portrays the expected results, a financial forecast. Therefore, only a financial forecast is appropriate for general use.

13.112 Limited use refers to use of the prospective financial information by a third party with whom the responsible party is negotiating directly, such as a bank negotiating with management for a loan. Third parties receiving limited-use prospective financial information can ask questions about the presentation. Therefore, projections or partial presentations as well as forecasts may be appropriate for limited use.

Use of the Information	Type of Information Appropriate	Type of Service	Type of Report
Internal Use Only	Any type of information, including a forecast, projection, or partial presentation	Any type of service, including compilation, examination, agreed-upon procedures, or assembly	Plain paper (no report) or assembly, compilation, examination, or agreed-upon procedures report
External Use General Use	Financial forecast	Compilation or examination	Compilation or examination
Limited Use	Financial forecast, projection, or partial presentation	Compilation, examination, or agreed-upon procedures	Compilation, examination, or agreed-upon procedures

13.200 DEVELOPING THE PROSPECTIVE FINANCIAL INFORMATION

13.201 Preparation of prospective financial information begins with the development of assumptions about all key factors that affect the future financial results of the entity. Many of the assumptions will be based on historical trends (for existing entities) and management's perspectives about the future.

13.202 Key factors vary by entity and industry, and they are often classified as being either external or internal, as described below:

External Factors:

- Economic conditions
- Industry conditions
- Actions of competitors
- Inflation rates
- Interest rates

Internal Factors:

- Sales level
- Collection activities
- Production activities
- Investing activities
- Financing activities

Sales

13.203 For all forecasts and projections, there is a factor that drives the prospective financial information. This factor is usually the demand for the entity's product or service, because the entity usually can produce more than it can sell. However, in some circumstances the productive capacity of the entity may determine the amount of product or service that may be sold. The following are a list of items to be considered in formulating the estimate of future sales:

- Past sales volume
- Trend in sales dollars and quantities
- Consumer demand and market trends
- Economic conditions that might affect the dollars and volume of sales, such as estimated future levels of personal income, employment, etc.
- Competition
- Pricing policies
- The extent and nature of the entity's marketing activities
- Sales incentives

In examining these items, the accountant is looking for internal and external changes in the business environment and relating those changes to expectations of future sales.

13.204 If the entity has several different types of products it may be more effective to develop the sales forecast by-product and aggregate the amounts to arrive at an overall estimate of future sales.

13.205 After the sales forecast for the year is developed, it may be necessary to allocate the sales to monthly periods. This is usually necessary when the entity is expected to have significant seasonal fluctuations in sales, because these fluctuations will significantly affect cash flow.

Billings and Collections

13.206 The next step in developing a forecast or projection involves developing an assumption about the average time it will take to collect sales. This assumption is usually based on historical information on past collections.

Other Cash Receipts

13.207 Assumptions should be formulated for anticipated collections of other revenues and other receivables, including:

- Investment revenue
- Interest revenue

- Rents and royalties
- Tax refunds
- Collections of other receivables
- Proceeds from sale of assets
- Proceeds from borrowings

Costs of Sales

13.208 Based on historical trends and plans of management, assumptions should be prepared about the quantity of production, the timing and amounts of purchases of raw materials, the quantity and price of labor, and inventory levels. For most elements of costs of sales, it is necessary to make several related assumptions, including the elements' costs, the period in which the costs will be incurred, and the period in which the payments will be made.

13.209 The timing and dollar amount of raw material purchases usually can be obtained by considering the pattern of forecasted sales and consideration of management plans. Past history also may be useful in this regard. With estimates of the entity's production, purchases and payment patterns, an estimate can be made of the timing and amounts of material purchases. Direct labor and overhead payments are estimated in a similar manner.

Other Expenses

13.210 Separate assumptions can be made about every other expense or group of expenses. In making these assumptions, it is often useful to analyze the historical behavior of costs to determine whether they are fixed, variable, or semi-variable. Consideration should also be given to inflationary increases and management plans.

13.211 Fixed expenses, such as rent, office salaries, and executive salaries do not vary over a wide range of activity. These expenses can usually be estimated by considering rent escalation clauses in lease agreements, proposed salary increases, purchases of new equipment, and labor agreements.

13.212 Variable expenses vary in direct proportion to some operating factor, such as sales volume, number of employees, or production levels. These expenses can be estimated based on the relationships between these factors and the related expenses.

13.213 Other expenses are semi-variable. A portion of a semi-variable expense is fixed and a portion is variable based on production. Examples of such expenses include supervision, maintenance, and utilities.

13.214 Some expenses are discretionary and solely determined by management's plans. Examples include employee bonuses, charitable contributions, advertising, and contributions to profit sharing plans. The amounts and timing of these expenditures must be estimated by management.

Other Disbursements

13.215 Other disbursements must also be estimated, including disbursements for purchases of assets and repayments of loans.

> **Practice Tip:**
>
> Even if the accountant assists management in developing the assumptions, it is important that management review and accept the assumptions. The assumptions must be consistent with management's plans.

Translating the Assumptions Into Financial Statements

13.216 Once the assumptions about the timing and amounts of cash disbursements are made, the accountant can assemble a statement of income and cash flows. A microcomputer spreadsheet is often useful for assembling these statements. Then, using the beginning balance sheet and the prospective statement of income and cash flows, the accountant can assemble the forecasted balance sheet for the entity.

> **Practice Tip:**
>
> The financial statements should be developed using the accounting principles expected to be used during the presentation's periods presented.

13.300 REASONABLY OBJECTIVE BASIS FOR THE PROSPECTIVE FINANCIAL STATEMENTS

13.301 The Guide requires the accountant to consider whether the responsible party has a reasonably objective basis for the prospective financial statements. In considering whether a reasonably objective basis exists, the accountant considers whether sufficiently objective assumptions can be developed for each key factor. Matters such as the following should be considered:

- The facts and informed judgments that can be obtained in support of the underlying assumptions.
- The subjectivity of significant assumptions.
- Whether knowledgeable people would select materially similar assumptions.
- The length of the forecast period.

Practice Tip:

The degree of uncertainty generally increases with the length of the period covered by the forecast. It would ordinarily be difficult to establish that a reasonably objective basis exists to present a forecast beyond three to five years.

13.302 When it is not practical to present a forecast for enough future periods to demonstrate long-term results of an investment decision, the entity's forecast may include a description of the potential results. For example, it may be appropriate to illustrate the planned sale of a real estate investment a number of years in the future. The disclosure should:

- Include an appropriate title.
- Indicate its purpose and that it is not a financial forecast.
- Include significant assumptions.
- State that it is presented for analysis purposes only and disclaim on the achievability of the results.

13.400 PRESENTATION GUIDELINES

13.401 The Guide includes the presentation guidelines for both forecasts and projections. These guidelines may be summarized as follows:

- The title of the prospective financial statement should be descriptive of the nature of the presentation (i.e., a forecast or projection). If the presentation is a projection the title should describe or refer to any significant hypothetical assumptions. For example, a projection that is contingent upon construction of an additional plant might be titled "Statement of Projected Results of Operations Assuming Construction of an Additional Plant."
- Prospective financial statements preferably should be in the format of the historical financial statements that would be issued for the period(s) covered.
- Prospective financial statements generally should be prepared using the accounting principles that are expected to be used in the period(s) presented.
- If some other comprehensive basis of accounting (OCBOA) is used by the client, the prospective financial statements should be prepared on that basis. Of course, the statement titles should be modified to reflect the other comprehensive basis of accounting used, e.g., "Statement of Forecasted Taxable Income."
- Prospective financial statements are normally expressed in specific monetary amounts as a single-point estimate of future results. However, the statements may be presented as a range of expected results, provided the range is not selected in a biased or misleading manner.

- The prospective financial statements should include a summary of significant assumptions that include:

  a. Assumptions about which there is a reasonable possibility of the occurrence of a variation that may significantly affect the future results, that is, sensitive assumptions.

  b. Assumptions about anticipated conditions that are expected to be significantly different from current conditions, which are not otherwise reasonably apparent.

  c. Other matters deemed important to the prospective information or its interpretation.

  d. In a projection, identification of the assumptions that are hypothetical, and disclosure of hypothetical assumptions deemed improbable.

- The summary of significant assumptions should identify which assumptions disclosed appeared particularly sensitive at the time of preparation. Particularly sensitive assumptions are those having a relatively high probability of variation that would materially affect the future results.

- The summary of assumptions should include an introduction that:

  a. Makes it clear that the assumptions disclosed are not all inclusive.

  b. Indicates what the prospective financial statements are intended to present.

  c. Includes a statement that the assumptions are based on the responsible party's judgment at the time the prospective information was prepared.

  d. Includes a caveat that the prospective results may not be attained.

  e. In a projection, the introduction also should clearly explain any special purpose and limitation of the usefulness of the statements.

- Ordinarily, the presentation should include at least one full year of normal operations.

- When prospective financial statements are presented with historical financial statements, the statements should be clearly labeled to distinguish them from the historical financial statements.

- Each page of the prospective financial statements should contain a reference to the summaries of significant assumptions and accounting policies.

13.500 SUGGESTIONS FOR IMPROVEMENT

13.501 Once a preliminary forecast or projection is completed, the accountant may have identified opportunities for management suggestions for improvement in operations. For example, policies may be implemented to improve the management of cash flows. Planned inventory levels may be reduced or better financing alternatives may be found. If management alters its plans based on these discussions, the prospective financial statements should be revised, accordingly.

13.600 CLIENT ACCEPTANCE

13.601 In considering whether to accept an engagement involving prospective financial information, the accountant should consider the factors described in section 3.002 of Chapter 3. Acceptance considerations are especially important when the services involve prospective financial statements. Prospective financial statements are developed from assumptions by the responsible party, and many of these assumptions are difficult or impossible to verify. Therefore, the integrity of the responsible party is essential to the presentation of reasonable prospective financial information.

> **Practice Tip:**
>
> Because of the potential legal liability involved in being associated with unreasonable prospective financial information, many accountants will perform these engagements only for existing clients.

13.700 PERFORMING PROSPECTIVE FINANCIAL STATEMENT ENGAGEMENTS

Performing a Plain Paper Engagement

13.701 A plain paper engagement is one in which an accountant performs one or more procedures on prospective financial information but does not report on the work performed. In addition, the accountant does not associate himself or herself with the presentation. To be defined as a plain paper engagement, the presentation must not refer to the accountant and should not be:

- Accompanied by an accountant's report or transmittal letter,
- Bound in the accountant's report cover,
- Printed on paper containing the accountant's logo or watermark,
- Bound with or alongside historical financial statements that are audited, reviewed, or compiled by the accountant.

13.702 Unless all of these conditions are met, the accountant is associated with the presentation and must, at a minimum, comply with the requirements for a transmittal letter (see section 13.703 below). An accountant may perform a plain paper engagement only on prospective financial statements for internal use only and partial presentations. If prospective financial statements are presented in an accountant-submitted document that also contains the accountant's compilation, review, or audit report on the entity's historical financial statements; the accountant is required to compile, examine, or apply agreed-upon procedures to the prospective financial statements.

13.703 **The Transmittal Letter.** In conveying prospective financial information on plain paper the accountant may decide to use a transmittal letter. The transmittal letter should include the following two caveats:

- A statement that the prospective financial statements are for internal use only.
- A statement that the prospective results may not be achieved.

13.704 Procedures for Plain Paper Engagements. When an accountant provides services on prospective financial statements for internal use, he or she should establish an understanding with the client, preferably in writing, regarding the services to be performed. This understanding should also specify that the prospective financial statements and the report, if any, are not to be distributed to outside users. Although the professional standards do not set forth the procedures to be performed in a plain paper engagement, the following are usually appropriate:

1. Obtain an understanding of the client's business and industry.
2. Specify the significant assumptions affecting the presentation.
3. Perform or test the computations used to translate the assumptions into the presentation.

Performing an Assembly Engagement

13.705 An assembly engagement is the lowest level of service an accountant should perform on internal-use prospective financial information or on a partial presentation when the accountant is associated with the information. An assembly engagement is similar to a plain paper service, except that the accountant issues a report on the work performed. Basically, an assembly is limited to performing or testing the mathematical accuracy of the computations that translate the assumptions into the prospective presentation.

13.706 When assembling prospective financial statements for internal use only, the accountant is required to obtain an understanding with the client, preferably in writing, of the type of services to be performed. The understanding should include a clear indication that the presentation and the accountant's report are for internal use only. Although the professional standards do not set forth the procedures to be performed in an assembly engagement, the following are usually appropriate:

- Obtain an understanding of the client's business and industry.
- Determine that the client has identified key factors affecting the prospective information.
- Determine that assumptions have been formulated for all key factors.
- Perform or test the computations that translate the assumptions into the prospective financial information.
- Prepare an assembly report.

Performing a Compilation Engagement

13.707 A compilation engagement is the lowest level of service an accountant can perform on prospective financial statements that are intended for use by third parties. A compilation of prospective financial statements is not equivalent to a compilation of financial statements under SSARS. More work is involved in the compilation of prospective financial statements because of the nature of prospective financial information.

13.708 The AICPA Audit and Accounting Guide, *Guide for Prospective Financial Information* includes the following standards that apply to a compilation engagement:

a. The compilation should be performed by a person or persons having adequate technical training and proficiency to compile a financial forecast (projection).

b. Due professional care should be exercised in the performance of the compilation and the preparation of the report.

c. The work should be adequately planned, and assistants, if any, should be properly supervised.

d. Applicable compilation procedures should be performed as a basis for reporting on the compiled financial forecast (projection).

e. The report based on the accountant's compilation of a financial forecast (projection) should be prepared in accordance with the guidance contained in the Guide.

13.709 **Planning the Engagement.** In planning a compilation engagement, the accountant should perform the following procedures:

1. Obtain an understanding of the client's industry including its accounting principles and practices.

2. Obtain a general knowledge of the nature of the client's business transactions, its accounting principles and practices, and the key factors upon which its future financial results appear to depend. This general knowledge may have been obtained in conjunction with other engagements performed for the client.

3. For a proposed company, the accountant should obtain knowledge of the proposed operations and the key factors upon which its future results appear to depend, and that have affected the performance of entities in the same industry.

Practice Tip:

If the accountant has no previous experience in the industry, he or she can obtain the required knowledge by consulting AICPA guides, industry publications, financial statements of other entities in the industry, textbooks, periodicals, or individuals knowledgeable about the industry.

13.710 Compilation Procedures. The following general procedures should be included in a compilation engagement:

1. Establish an understanding with the client, preferably in writing, of the nature of the services to be performed.

2. Inquire about the accounting principles used in the preparation of the prospective financial statements.

3. Inquire about how the responsible party identifies key factors and develops assumptions.

4. Develop a list of the significant assumptions and consider whether there are any obvious omissions in light of the key factors upon which the client's prospective results appear to depend.

5. Consider whether there appear to be any obvious internal inconsistencies in the assumptions. (For example, the use of a high future inflation rate and a low future interest rate.)

6. Perform or test the mathematical accuracy of the computations that translate the assumptions into the prospective financial statements.

7. Read the prospective financial statements, including the summary of significant assumptions, and consider whether:

   - The prospective financial statements, including the summary of significant assumptions and accounting policies, appear to be presented in conformity with the AICPA presentation guidelines for prospective financial statements in the Guide.
   - The prospective financial statements, including the summary of significant assumptions, appear to be not obviously inappropriate in relation to:

     a. The accountant's knowledge of the entity and its industry.

     b. The expected conditions and course of action in the prospective financial statements.

8. If the presentation is a financial projection, the accountant should consider whether the projection appears to be obviously inappropriate in relation to the special purpose of the presentation.

9. If a significant part of the prospective period has expired, inquire about the results of operations or significant portions of the operations (such as sales volume) and significant changes in financial position, and consider their effect in relation to the prospective financial statements. If historical financial statements have been prepared for the expired portion of the period, the accountant should read such statements and consider those results in relation to the prospective financial statements.

10. Obtain a representation letter from the responsible party in which that party indicates its responsibility for the assumptions. The letter should be signed by the responsible party at the highest level of authority who the accountant believes is responsible for and knowledgeable about matters covered by the representations.

    - If the presentation is a financial forecast, the representation letter should include a statement that the financial forecast presents, to the best of the responsible party's knowledge and belief, the expected financial position, results of operations, and cash flows for the forecast period, and that the forecast reflects the responsible party's judgment, based on present circumstances, of the expected conditions and its expected course of action.
    - If the presentation is a financial projection, the representation letter should include a statement that the financial projection presents, to the best of the responsible party's knowledge and belief, the expected financial position, results of operations, and cash flows for the projection period given the hypothetical assumptions, and that the projection reflects its judgment, based on present circumstances, of expected conditions and its expected course of action given the occurrence of the hypothetical events. The representation letter should also: (1) identify the hypothetical assumptions and describe the limitations on the usefulness of the presentation, (2) state that the assumptions are appropriate, and (3) indicate if the hypothetical assumptions are improbable.
    - If the prospective financial statements are presented as a range, the representation letter should include an indication that, to the best of the responsible party's knowledge and belief, the item or items (given any hypothetical assumptions) are expected to actually fall within the range and that the range was not selected in a biased or misleading manner.

11. Consider whether representations or other information has been received that appears to be obviously inappropriate, incomplete, or otherwise misleading. If so, attempt to obtain additional or revised information. If revised information is not provided, consider withdrawing from the engagement.

12. Prepare a compilation report.

Practice Tip:

The procedures for a compilation of a partial presentation are essentially the same as those for complete prospective financial statements. However, the procedures are applied only to those assumptions and disclosures that are relevant to the partial presentation.

13.711 Reporting on a Compilation Engagement. A compilation report on prospective financial statements should include:

- A specific identification of the prospective financial statements presented.

- A paragraph that describes the limitations of the usefulness of the presentation, if the presentation is a projection.
- A statement that the accountant has compiled the prospective financial statements in accordance with standards established by the American Institute of Certified Public Accountants.
- A statement that a compilation is limited in scope and does not enable the accountant to express an opinion or any other form of assurance on the prospective financial statements or the assumptions.
- A caveat that the forecasted results may not be achieved.
- A statement that the accountant has no responsibility to update the report for events or circumstances occurring after the date of the report.

13.712 When the prospective financial statements contain a range, the accountant's report should also include a separate paragraph that states that the responsible party has elected to present the expected results of one or more assumptions as a range.

13.713 The report should be dated as of the date of completion of the accountant's compilation procedures.

13.714 Modifications of the Compilation Report. The accountant's compilation report should be modified in the following circumstances:

- When the accountant is not independent, the report should include the following as the last paragraph:

  "I am (We are) not independent with respect to XYZ Company."

- When the prospective financial statements are accompanied by historical financial statements, the accountant should also report on the historical financial statements.
- When the prospective financial statements contain presentation deficiencies or omit disclosures (other than those relating to significant assumptions), the report should be modified to describe the deficiencies or omissions.
- When the compiled prospective financial statements are presented on a comprehensive basis of accounting other than generally accepted accounting principles and does not include disclosure of the basis of accounting used, the basis should be disclosed in the compilation report.
- When the accountant wishes to emphasize a matter related to the prospective financial statements.

Practice Tip:

The accountant cannot report on prospective financial statements that omit the summary of significant assumptions.

Working Papers

13.715 The accountant's working papers ordinarily should show that:

- The work was adequately planned and supervised.
- The required compilation procedures were performed as a basis for the compilation report.

13.716 Table 13-1 illustrates suggested working papers for documentation of an engagement for compilation of prospective financial information. The Documentation section of this chapter includes forms, checklists, and work programs for performing compilation engagements on prospective financial information, including:

1. Engagement Letter — Compilation of Forecast (Projection).
2. Compilation Work Program — Prospective Financial Statements.
3. Representation Letter — Compilation of Financial Forecast (Projection).
4. Form for Presentation of Prospective Financial Statements.

Table 13-1

Suggested Working Papers for Compilation Engagement — Prospective Financial Information

Section	Description
13.901 and 13.902	Engagement Letter or Memorandum Describing Understanding With the Client
3.501	Client Acceptance and Continuance Form
3.502	Form for Documenting Understanding of Client's Business and Industry — Compilation and Review Engagements
13.904	Compilation Work Program — Prospective Financial Statements
13.905	Form for Presentation of Prospective Financial Statements
13.906 and 13.908	Representation Letter — Compilation of Financial Forecast (Projection)

13.800 ILLUSTRATIVE PROSPECTIVE FINANCIAL STATEMENTS AND DISCLOSURES

XYZ COMPANY, INC.

Forecasted Statement of Income and Retained Earnings
Year Ending December 31, 19X3
(in thousands except per share amounts)

	Forecasted 19X3	Comparative Historical Information 19X2	19X1
Net sales	$101,200	$91,449	$79,871
Cost of sales	77,500	70,140	60,463
Gross profit	23,700	21,309	19,408
Selling, general, and administrative expenses	15,100	13,143	11,014
Operating income	8,600	8,166	8,394
Other income (deductions):			
Miscellaneous	1,700	964	(308)
Interest expense	(2,400)	(1,914)	(1,943)
	(700)	(950)	(2,251)
Income before income taxes	7,900	7,216	6,143
Income taxes	3,400	3,267	2,929
Net Income	4,500	3,949	3,214
Retained earnings at beginning of year	10,500	7,803	5,543
Dividend (per share 19X3: $1.50; 19X2: $1.35; 19X1: $1.00)	(1,400)	(1,288)	(954)
Retained earnings at end of year	$ 13,600	$10,464	$ 7,803
Net income per share	$ 4.73	$ 4.14	$ 3.37

See accompanying Summary of Significant Forecast Assumptions and Accounting Policies.

XYZ COMPANY, INC.

Forecasted Statement of Cash Flows
Year Ending December 31, 19X3
(in thousands)

	Forecasted	Comparative Historical Information	
	19X3	19X2	19X1
Cash Flows From Operating Activities:			
Net income	$4,500	$3,949	$3,214
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation Expense	2,800	2,422	2,181
Changes in:			
Accounts receivable	(2,500)	(1,430)	(483)
Inventory	(100)	(3,995)	(1,431)
Other current assets	(1,700)	(350)	(62)
Accounts payable and accrued expenses	1,100	1,696	846
Other current liabilities	—	811	161
Net cash provided by operating activities	4,100	3,103	4,426
Cash Flows (Used For) Investing Activities:			
Additions to property and equipment	(4,400)	(2,907)	(2,114)
Other assets	(2,200)	(600)	(83)
Net cash used for investing activities	(6,600)	(3,507)	(2,197)
Cash Flows From (Used For) Financing Activities:			
Dividends paid	(1,400)	(1,288)	(954)
Proceeds from bank loans	1,500	100	(300)
Proceeds from long-term borrowings	6,000	4,100	2,000
Principal payments of long-term debt	(2,200)	(2,842)	(1,958)
Net cash from (used in) financing activities	3,900	70	(1,212)
Net increase (decrease) in cash	1,400	(334)	1,017
Cash, beginning of year	1,900	2,196	1,179
Cash, end of year	$ 3,300	$ 1,862	$ 2,196

Income tax payments were $3,207 and $2,789 in 19X2 and 19X1, respectively, and are estimated to be $3,300 in 19X3. Interest payments related to borrowings were $1,756 and $2,155 in 19X2 and 19X1, respectively, and are estimated to be $2,620 in 19X3.

See accompanying Summary of Significant Forecast Assumptions and Accounting Policies.

XYZ COMPANY, INC.

Forecasted Balance Sheet
December 31, 19X3
(in thousands)

	Forecasted	Comparative Historical Information	
	19X3	19X2	19X1
ASSETS			
Current Assets:			
Cash	$ 3,300	$ 1,862	$ 2,196
Accounts receivable (net)	14,900	12,438	11,008
Inventory	27,000	26,932	22,937
Other	3,500	1,813	1,463
Total current assets	48,700	43,045	37,604
Property, plant, and equipment	30,900	26,915	22,832
Less accumulated depreciation	17,300	14,912	11,314
Net property, plant, and equipment	13,600	12,003	11,518
Other assets	5,000	2,714	2,114
	$67,300	$57,762	$51,236
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current Liabilities:			
Notes payable to bank	$ 4,600	$ 3,100	$ 3,000
Accounts payable and accrued expenses	12,300	11,193	9,497
Current installments of long-term debt	4,400	3,968	3,010
Other	900	925	114
Total current liabilities	22,200	19,186	15,621
Long-term debt, excluding current installments	20,100	16,700	16,400
Stockholders' Equity:			
Capital stock	11,400	11,412	11,412
Retained earnings	13,600	10,464	7,803
Total stockholders' equity	25,000	21,876	19,215
	$67,300	$57,762	$51,236

See accompanying Summary of Significant Forecast Assumptions and Accounting Policies.

XYZ COMPANY, INC.

Summarized Financial Forecast
Year Ending December 31, 19X3
(in thousands except per share amounts)

Following is a summarized presentation that could be used in lieu of the preceding three statements.

	Forecasted	Comparative Historical Information*	
	19X3	19X2	19X1
Sales	$101,200	$ 91,449	$ 79,871
Gross profit	23,700	21,309	19,408
Income tax expense	3,400	3,267	2,929
Net income	4,500	3,949	3,214
Net income per share	4.73	4.14	3.37
Significant Anticipated Changes in Financial Position:			
Cash provided by operations	4,100	3,103	4,426
Net increase (decrease) in long-term borrowings	3,400	300	(300)
Dividend (per share 19X3: $1.50; 19X2: $1.35; 19X1: $1.00)	1,400	1,288	954
Additions to plant and equipment	4,400	2,907	2,114
Increase (decrease) in cash	1,400	(334)	1,017

See accompanying Summary of Significant Forecast Assumptions and Accounting Policies.

* Comparative historical information is not part of the required minimum presentation.

XYZ COMPANY, INC.

Summary of Significant Forecast Assumptions and Accounting Policies
Year Ending December 31, 19X3

This financial forecast presents, to the best of management's knowledge and belief, the Company's expected financial position, results of operations, and cash flows for the forecast period.* Accordingly, the forecast reflects management's judgment as of February 17, 19X3, the date of this forecast, of the expected conditions and its expected course of action. The assumptions disclosed herein are those that management believes are significant to the forecast. There will usually be differences between forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. The comparative historical information for 19X1 and 19X2 is extracted from the Company's financial statements for those years. Those financial statements should be read for additional information.

a. *Summary of Significant Accounting Policies* (not illustrated).

b. *Sales.* The overall market for the Company's products has grown over the past five years at an average rate of 2% above the actual increase in gross national product, and the Company's market share has remained steady at 14% to 16%. Based on a recent market study of demand for the Company's products, sales are forecasted to increase 11% from 19X2 (which is 2% above the Department of Commerce Bureau of Economic Analysis estimate of the rise in gross national product in the forecast period), with a market share of 15% and unit price increase to cover a significant portion of forecasted increases in cost of manufacturing.

c. *Cost of Sales*

Materials. Materials used by the Company are expected to be readily available, and the Company has generally used producer associations' estimates of prices in the forecast period to forecast material costs. The price for copper, a major raw material in the Company's products, recently has been disrupted by political events in certain principal producer countries. As a result, industry estimates of copper prices in the forecast period range from 15% to 30% above 19X2 prices. The Company expects to be able to assure sufficient supplies and estimates that the cost of copper will increase by 22% over 19X2. However, due to the uncertainties noted above, the realization of the forecast is particularly sensitive to the actual price increase. A variation of five percentage points in the actual increase above or below the assumed increase would affect forecasted net earnings by approximately $485,000.

Labor. The Company's labor union contract, which covers substantially all manufacturing personnel, was negotiated in 19X2 for a three-year period. Labor costs are forecasted based on the terms of that contract.

---

* For the presentation illustrated on page 13-29, this would read "...summary of the Company's expected results of operations and changes in financial position...."

d. *Plant and Equipment and Depreciation Expense.* Forecasted additions to plant and equipment, $4.4 million, comprise principally the regular periodic replacement of manufacturing plant and vehicles at suppliers' quoted estimated prices and do not involve a significant change in manufacturing capacity or processes. Depreciation is forecasted on an item-by-item basis.

e. *Selling, General, and Administrative Expenses.* The principal types of expense within this category are salaries, transportation costs, and sales promotion. Salaries are forecasted on an individual-by-individual basis, using expected salary rates in the forecast period. Transportation costs comprise principally the use of contract carriers; volume is forecasted based on the sales and inventory forecasts (including forecasts by sales outlet), and rates are forecasted to rise by 16% over 19X2, based on trucking industry forecasts. Sales promotion costs are expected to increase by approximately 14% above the level of 19X2 in order to meet increased competition and to maintain market share. The level of other expenses is expected to remain the same as in 19X2, adjusted for expected increases in line with the consumer price index (assumed to rise 9% on the means of [*several widely used estimates*]).

f. *Miscellaneous Income.* The forecast assumes royalty income of $950,000 will be received based on an agreement under which the Company is to receive a minimum of $950,000 for the first 10,000,000 units produced under its patented die casting process and $.05/unit above that level. Management believes it is unlikely that production will exceed 10,000,000 units. The balance of miscellaneous income is assumed to come from investment of excess cash and other sources.

g. *Bank Borrowings and Interest Expense.* The forecast assumes that the Company will obtain an extension of existing short-term lines of credit at terms comparable to those in effect in 19X2 (T% over prime rate). The Company used the arithmetic means of [*three widely used estimates*] bank prime rate during the forecast period (ranging from X% to Y%) to estimate prime rate at Z%. However, because of recent volatility in the financial markets, short-term interest rates have been very unstable, ranging from X% to Y% during 19X2.

The Company has forecasted additional long-term borrowings of $6 million and has entered into preliminary negotiations with its bankers for this financing. The borrowings are principally to fund purchases of plant and equipment and additions to other long-term assets and will be secured by such additions. Based on the preliminary negotiations, the Company has assumed that the additional long-term financing will bear interest at A%.

h. *Income Taxes.* The provision for income taxes is computed using the statutory rates in effect during 19X2, which are not expected to change, and assuming investment tax credit on qualifying investments at rates in effect in 19X2.

i. *Dividend.* The Company's normal dividend policy is to pay out the previous year's dividend increased to the extent of at least one-third of any increase in profits over the previous year, provided the board of directors considers that the Company's cash and working capital position will not be adversely affected. The dividend has been forecasted at $1.50 per share, assuming an increased payout over 19X2 of one-third of the excess of forecasted net earnings for the year ending December 31, 19X3, above those in 19X2.

ABC COMPANY, INC.
Statement of Projected Results of Operations and Cash Flow
Assuming Construction of an Additional Plant
For Each of the Five Years Ending December 31, 19X7
(in thousands except per share amounts)

	Year Ending December 31,				
	19X3	19X4	19X5	19X6	19X7
Net sales	$101,200	$112,300	$142,000	$156,200	$173,400
Cost of sales	77,500	86,100	109,300	120,100	133,300
Gross profit	23,700	26,200	32,700	36,100	40,100
Selling, general, and administrative expenses	15,100	16,500	19,500	21,400	23,400
Operating income	8,600	9,700	13,200	14,700	16,700
Other income (deductions):					
Miscellaneous	1,700	1,200	1,000	1,300	1,800
Interest expense	(2,400)	(3,500)	(3,400)	(3,200)	(3,000)
	(700)	(2,300)	(2,400)	(1,900)	(1,200)
Income before taxes	7,900	7,400	10,800	12,800	15,500
Income taxes	3,400	2,800	4,700	5,500	6,700
Net income	4,500	4,600	6,100	7,300	8,800
Add noncash expenses:					
Depreciation and amortization	2,800	2,800	3,400	3,500	3,500
Deferred taxes	500	450	550	600	650
	7,800	7,850	10,050	11,400	12,950
Add (deduct)					
Loan proceeds for additional plant facility	8,500	1,500	—	—	—
Increase in excess of receivables and other assets over payables	(1,000)	(1,000)	(2,000)	(3,000)	(3,500)
Cash requirements for building costs	(8,200)	(1,800)	—	—	—
Other additions to plant and equipment	(3,400)	(2,200)	(2,200)	(2,200)	(2,200)
Cash requirements for repayment of debt	(2,600)	(2,600)	(3,700)	(3,500)	(3,500)
Dividends	(1,400)	(1,400)	(1,900)	(2,200)	(2,700)
Increase (decrease) in cash	(300)	350	250	500	1,050
Cash, beginning of year	3,300	3,000	3,350	3,600	4,100
Cash, end of year	$ 3,000	$ 3,350	$ 3,600	$ 4,100	$ 5,150
Net income per share	$ 4.80	$ 4.92	$ 6.51	$ 7.79	$ 9.39
Dividends per share	$ 1.50	$ 1.50	$ 2.03	$ 2.35	$ 2.88

See accompanying Summary of Significant Forecast Assumptions and Accounting Policies.

ABC COMPANY, INC.

Summary of Significant Assumptions Employed in Preparation of the Statement of Projected Results of Operations and Cash Flow Assuming Construction of an Additional Plant For Each of the Years Ending December 31, 19X7

This financial projection of operations and cash flow assuming construction of an additional plant presents, to the best of management's knowledge and belief, the expected results of operations and cash flow for the projection period if a plant were constructed to increase production capacity by approximately 20%. Accordingly, the projection reflects management's judgment as of October 24, 19X2, the date of this projection, of the expected conditions and its expected course of action if such a plant were constructed. The presentation is designed to provide information for potential bank financing of the construction of the additional plant and cannot be considered to be a presentation of expected future results. Accordingly, this projection may not be useful for other purposes. The assumptions disclosed herein are those that management believes are significant to the projection; however, management has not decided that it will construct such a plant. Even if the plant were constructed, there will usually be differences between projected and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material.

a. *Summary of Significant Accounting Policies* (not illustrated).

b. *Hypothetical Assumption — Increase in Production Capacity by Construction of a New Plant.* The projection is based on the assumption that production capacity will be increased by approximately 20% by the construction of a 160,000 square foot production facility in Richmond, Virginia.

   Construction on the new plant is projected to begin in February 19X3 and to be completed by June 30, 19X4, at a total cost of $10,000,000 including construction-period interest of $1,300,000. Production cost estimates and the projected completion date have been estimated based on competitive bids received.

   The decision to proceed with the project and the awarding of contracts will depend on the completion of financing arrangements.

c. *Sales.* The overall market for the Company's products has grown over the past five years at an average rate of 2% above the actual increase in gross national product, and the Company's market share has remained steady at 14% to 16%. Based on a recent market study of demand for the Company's products, sales are projected to increase 11% per annum from 19X2 to 19X4 (which is consistent with a rate of 2% above the Department of Commerce Bureau of Economic Analysis' estimate of the rise in gross national product in the projection period), with a market share of 15% and unit prices increased to cover projected increases in cost of manufacturing. Based on the study, an additional 15% increase in sales is projected to occur beginning in 19X5 and will be met by the added capacity resulting from the plant expansion.

d. *Costs of Sales*

Materials. Materials used by the Company are expected to be readily available, and the Company has generally used producer associations' estimates of prices in the projection period to project material costs. The Company expects to be able to assure a sufficient supply of materials and estimates that the cost of materials will increase by 12% per annum.

Labor. The Company's labor union contract, which covers substantially all manufacturing personnel, will be subject to renegotiation in 19X6. Labor costs until that time are projected based on the existing contract. For 19X7, labor costs, including fringe benefits, are projected to increase 19% per year above the 19X6 level. The outcome of the projection is particularly sensitive to variances in such labor costs. For each percentage point variance from the projected increase, net income and cash will vary by approximately $380,000.

e. *Plant and Equipment and Depreciation Expense*. Projected additions to plant and equipment, other than the assumed plant expansion, are principally the regular periodic replacement of manufacturing plant and vehicles at suppliers' quoted estimated prices and do not involve any significant changes in manufacturing capacity or processes. Depreciation is projected on an item-by-item basis. Depreciation on the new facility is projected on a straight-line basis over 20 years.

f. *Selling, General, and Administrative Expense*. The principal types of expenses within this category are salaries, transportation costs, and sales promotion. Salaries are projected on an individual-by-individual basis, using expected salary rates in the projection period. Transportation costs are principally for contract carriers; volume is projected based on sales and inventory projections, and rates are forecasted by 16% per year based on trucking industry forecasts. Sales promotion costs are expected to increase in line with the consumer price index, as is the level of other expenses.

g. *Bank Borrowings and Interest Expense*. The projection assumes that the Company will obtain an extension of existing short-term lines of credit at terms comparable to those in effect in 19X2 (2% over prime rate). The Company used the arithmetic mean of [*three widely used estimates*] bank prime rate during the projection period (ranging from X% to Y%) to estimate prime rate at Z%. The Company projects additional long-term borrowing of $10 million to finance the planned plant expansion (including $1,300,000 of construction-period capitalized interest) and has entered into preliminary negotiations with its bankers for this financing. Based on the preliminary negotiations, the Company has assumed that the additional long-term financing will bear interest at Y%.

h. *Miscellaneous Income*. The projection assumes that royalty income of $950,000 will be received annually based on an agreement under which the Company is to receive a minimum of $950,000 for the first 10,000,000 units produced under its patented die casting process and $.05/unit above that level. Management believes it is unlikely that production will exceed 10,000,000 units and any of the projection periods.

i. *Income Taxes*. The provision for income taxes is computed using the statutory rates in effect during 19X2, which are not expected to change. The Company anticipates that it will take investment tax credits on the machinery and equipment to be installed in the new plant when the plant is placed in service in 19X4.

j. *Dividend.* The Company's normal dividend policy is to pay out the previous year's dividend increased to the extent of at least one-third of any increase in profits over the previous year, provided the board of directors considers that the Company's cash and working-capital position will not be adversely affected.

13.900 DOCUMENTATION ASSISTANCE

13.901 Engagement Letter — Compilation of a Forecast

[Client's Letterhead]

____
____
____

This letter is to confirm my (our) understanding of the terms and objectives of my (our) engagement, and the nature and limitations of the services I (we) will provide.

I (We) will perform the following services:

I (We) will compile, from information you provide, a forecasted balance sheet and the related forecasted statements of earnings, retained earnings, and cash flows of ____________ [client name] as of ______ [forecast date] and for the year then ending. I (We) will not express any form of assurance on the achievability of the forecast, or on the reasonableness of the underlying assumptions. My (Our) standard report on the compilation of your forecasted financial statements reads as follows:

> We have compiled the accompanying forecasted balance sheet and the related forecasted statements of income, retained earnings, and cash flows of _______[client name] as of _____ [balance-sheet date], and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants.
>
> A compilation is limited to presenting in the form of a forecast information that is the representation of management and does not include evaluation of the support for the assumptions underlying the forecast. We have not examined the forecast and, accordingly, do not express an opinion or any other form of assurance on the accompanying statements or assumptions. Furthermore, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events or circumstances occurring after the date of this report.[1]

---

[1] If the financial statements will omit the summary of significant accounting policies, the following should be added:

My (Our) standard form compilation report on your forecasted financial statements, which omit substantially all disclosures, includes an additional paragraph that reads as follows:

> Management has elected to omit the summary of significant accounting policies required by the guidelines for presentation of a forecast established by the American Institute of Certified Public Accountants. If the omitted disclosures were included in the forecast, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows for the forecasted period. Accordingly, this forecast is not designed for those who are not informed about such matters.

If, for any reason, I am (we are) unable to complete the compilation of the forecasted financial statements, I (we) will not issue a report on such statements as a result of this engagement.

Management is responsible for representations about its plans and expectations and for disclosure of significant information that might affect the ultimate realization of the forecasted results.

Furthermore, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and such differences may be material.

I (We) have no responsibility to update my (our) report for events and circumstances occurring after the date of my (our) report.

In order for me (us) to complete this engagement, management must provide assumptions that are appropriate for the forecast. If the assumptions provided are inappropriate and have not been revised to my (our) satisfaction, I (we) will be unable to complete the engagement and, accordingly, I (we) will not issue a report on the forecast.

My (Our) fees will be billed as work progresses and are based on the amount of time required plus out-of-pocket expenses. Invoices are payable upon presentation. I (We) will notify you immediately of any circumstances I (we) encounter that could significantly affect my (our) initial estimate of total fees, which will range from $____ to $____.

If this letter correctly expresses your understanding, please sign the enclosed copy where indicated and return it to me (us).

I (We) appreciate the opportunity to serve you and trust that our association will be a long and pleasant one.

Sincerely,

____
[Engagement Partner's Signature]

____
[Date]

Accepted and agreed to:

____
[Client's Representative's Signature]

____
[Title]

____
[Date]

13.902 Engagement Letter — Compilation of a Projection

[Client's Letterhead]

____

____

____

This letter is to confirm my (our) understanding of the terms and objectives of my (our) engagement, and the nature and limitations of the services I (we) will provide.

I (We) will perform the following services:

I (We) will compile, from information you provide, a projected balance sheet and the related projected statements of earnings, retained earnings, and cash flows of ____________ [client name] as of _____ [projection date] and for the year then ending. I (We) will not express any form of assurance on the achievability of the projection, or on the reasonableness of the underlying assumptions. My (Our) standard report on the compilation of your projected financial statements reads as follows:

> We have compiled the accompanying projected balance sheet and the related projected statements of income, retained earnings, and cash flows of ______[client name] as of _____ [balance-sheet date], and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants.
>
> The accompanying projection and this report were prepared for [state purpose of the projection] and should not be used for any other purpose.
>
> A compilation is limited to presenting in the form of a projection information that is the representation of management and does not include evaluation of the support for the assumptions underlying the projection. We have not examined the projection and, accordingly, do not express an opinion or any other form of assurance on the accompanying statements or assumptions. Furthermore, even if [describe hypothetical assumption] there will usually be differences between the projected and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events or circumstances occurring after the date of this report.[1]

---

[1] If the financial statements will omit the summary of significant accounting policies the following should be added to the engagement letter:

My (Our) standard form compilation report on your projected financial statements, which omit substantially all disclosures, includes an additional paragraph that reads as follows:

> Management has elected to omit the summary of significant accounting policies required by the guidelines for presentation of a projection established by the American Institute of Certified Public Accountants. If the omitted disclosures were included in the projection, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows for the projection period. Accordingly, this projection is not designed for those who are not informed about such matters.

If, for any reason, I am (we are) unable to complete the compilation of the projected financial statements, I (we) will not issue a report on such statements as a result of this engagement.

Management is responsible for representations about its plans and expectations and for disclosure of significant information that might affect the ultimate realization of the projected results.

Furthermore, there will usually be differences between the projected and actual results, because events and circumstances frequently do not occur as expected, and such differences may be material.

I (We) have no responsibility to update my (our) report for events and circumstances occurring after the date of my (our) report.

In order for me (us) to complete this engagement, management must provide assumptions that are appropriate for the projection. If the assumptions provided are inappropriate and have not been revised to my (our) satisfaction, I (we) will be unable to complete the engagement and, accordingly, I (we) will not issue a report on the projection.

My (Our) fees will be billed as work progresses and are based on the amount of time required plus out-of-pocket expenses. Invoices are payable upon presentation. I (We) will notify you immediately of any circumstances I (we) encounter that could significantly affect my (our) initial estimate of total fees, which will range from $____ to $____.

If this letter correctly expresses your understanding, please sign the enclosed copy where indicated and return it to me (us).

I (We) appreciate the opportunity to serve you and trust that our association will be a long and pleasant one.

Sincerely,

____

[Engagement Partner's Signature]

____

[Date]

Accepted and agreed to:

____

[Client's Representative's Signature]

____

[Title]

____

[Date]

13.903

Work Program — Prospective Financial Statements for Internal Use Only

Client: ____________________

Prospective Financial Statement Date: ____________________

INSTRUCTIONS:

This checklist includes the procedures suggested for the performance of services on prospective financial statements for internal use only.

	Performed By		
	Initials	Date	N/A
1. Prepare or update the Client Acceptance and Continuance Form.	______	______	☐
2. Obtain an understanding of the services to be provided, and that the presentation will not be used by a third party.	______	______	☐
3. Review any working paper files from other engagements for this client as considered necessary.	______	______	☐
4. Meet with the client and discuss the following:			
a. The intended use and nature of the presentation.	______	______	☐
b. Key factors affecting the entity's future operations.	______	______	☐
5. Prepare a list of assumptions for all key factors affecting the entity's future operations.	______	______	☐
6. Perform or test the mathematical accuracy of computations that translate the assumptions into the presentation.	______	______	☐

WORK PROGRAM — PROSPECTIVE FINANCIAL STATEMENTS FOR INTERNAL USE ONLY (Continued)

	Performed By		
	Initials	Date	N/A
7. Prepare the presentation using the guidelines contained in the AICPA Guide.			
a. The title used for the prospective financial statements should be descriptive of the nature of the presentation (forecast or projection). For a projection, the title should describe or refer to any significant hypothetical assumptions.	________	________	☐
b. The title should indicate the date of the presentation using the word "ending," for example, "Year ending December 31, 19XX."	________	________	☐
c. When the historical financial statements that will be issued for the prospective period are expected to be prepared in conformity with OCBOA, the prospective financial statements should preferably be prepared on that basis and appropriately titled.	________	________	☐
8. If the prospective financial statements are to be presented on plain paper, determine that the accountant's name is not in any way associated with the presentation. (Although the summary of significant assumptions may be omitted from plain paper presentations, it is not recommended.)	________	________	☐
9. If an assembly report is issued, determine that the presentation includes both the summary of significant assumptions and accounting policies.	________	________	☐
10. If an assembly report is to be presented, make modifications in the following circumstances:			
a. Lack of independence.	________	________	☐
b. Sensitive assumptions not identified.	________	________	☐

WORK PROGRAM — PROSPECTIVE FINANCIAL STATEMENTS FOR INTERNAL USE ONLY (Continued)

	Performed By: Initials	Performed By: Date	N/A
c. Omission of significant accounting policies.	______	______	☐
d. Other disclosures required by AICPA presentation guidelines are omitted.	______	______	☐
e. The prospective statements are presented with historical statements.	______	______	☐
11. Determine that each page of the presentation refers to the summary of significant assumptions and accounting policies.	______	______	☐
12. Document any other procedures performed or unusual problems and their resolution.	______	______	☐
13. Determine that all review points by the engagement team and the technical reviewer (if applicable) have been resolved.	______	______	☐

Prepared by: ______________________ Date: ______________
(In-Charge)

Reviewed by: ______________________ Date: ______________
(Partner)

13.904

Compilation Work Program — Prospective Financial Statements

Client: ______________________________

Prospective Financial Statement Date: ______________________________

INSTRUCTIONS:

The following is a general guide for compiling prospective financial statements. Any additional inquiries or procedures performed, and conclusions reached, should also be documented in the working papers. The "N/A" column should be checked for any steps that are not applicable or for steps not required because of immateriality or other reasons. References are to the AICPA *Guide for Prospective Financial Information*.

This WORK PROGRAM should be used on compilation engagements in connection with the following documents:

1. Client Acceptance and Continuance Form.

2. Form for Documenting Understanding of Client's Business and Industry — Compilation and Review Engagements.

	Performed By		
	Initials	Date	N/A
1. Prepare or update the Client Acceptance and Continuance Form.	________	________	☐
2. Establish or update an understanding with the client, preferably in writing, regarding the nature of the engagement. Include in the working papers a copy of the engagement letter or a memorandum describing the oral arrangements. [AAG-PRO 12.10]	________	________	☐
3. Complete or update the Form for Documenting Understanding of Client's Business and Industry — Compilation and Review Engagements. [AAG-PRO 12.06-12.07]	________	________	☐

COMPILATION WORK PROGRAM — PROSPECTIVE FINANCIAL STATEMENTS (Continued)

	Performed By		
	Initials	Date	N/A
4. Review any working paper files from other engagements for this client as considered necessary.	______	______	☐
5. Meet with client and discuss the following [AAG-PRO 12.10]:	______	______	☐
a. The intended use and nature of the presentation.	______	______	☐
b. Key factors affecting the company's future operations.	______	______	☐
c. How the client identifies the factors and assumptions.	______	______	☐
6. Consider whether the staffing and scheduling of the engagement is appropriate.	______	______	☐
7. Obtain or prepare a list of assumptions for all key factors affecting the company's future operations. Consider whether there is a reasonably objective basis for all assumptions. [AAG-PRO 12.10]	______	______	☐
8. Perform or test the mathematical accuracy of the computations that translate the assumptions into the presentation. [AAG-PRO 12.10]	______	______	☐
9. Consider whether there appear to be any obvious internal inconsistencies in the assumptions. [AAG-PRO 12.10]	______	______	☐
10. Read the financial presentation, including the summary of significant assumptions, and consider whether: [AAG-PRO 12.10]	______	______	☐
a. The presentation, including disclosures of assumptions and accounting policies, appears to be presented in conformity with AICPA presentation guidelines.	______	______	☐
b. The presentation, including the summary of significant assumptions, appears to be appropriate in relation to your knowledge of the client and its industry.	______	______	☐

COMPILATION WORK PROGRAM—PROSPECTIVE FINANCIAL STATEMENTS (Continued)

	Performed By Initials	Date	N/A
c. The presentation, including the summary of significant assumptions, appears to be appropriate in relation to:	________	________	☐
i. The expected conditions and course of action for a forecast, or	________	________	☐
ii. The special purpose of a projection.	________	________	☐
11. If a significant part of the prospective period has expired, inquire about the results of operations and significant changes in financial position and consider their effect in relation to the presentation. [AAG-PRO 12.10]	________	________	☐
12. Read any historical statements prepared for expired portions of the period. [AAG-PRO 12.10]	________	________	☐
13. Obtain a client representation letter. [AAG-PRO 12.10]	________	________	☐
14. If any representation or other information appears to be obviously inappropriate, incomplete, or otherwise misleading, obtain additional or revised information. If such information cannot be obtained, consider withdrawing from the engagement. [AAG-PRO 12.10]	________	________	☐
15. Prepare a compilation report. Make modifications in the following circumstances:			
a. Lack of independence. [AAG-PRO 14.05]	________	________	☐
b. Omission of significant accounting policies. [AAG-PRO 14.09-.10	________	________	☐
c. The presentation departs in any other way from the presentation guidelines of the AICPA Guide. [AAG-PRO 14.09-.10]	________	________	☐
d. Partial presentations that require a description of purpose and limitations on the usefulness of the information. [AAG-PRO 23.22-23.23]	________	________	☐

COMPILATION WORK PROGRAM — PROSPECTIVE FINANCIAL STATEMENTS (Continued)

	Performed By		
	Initials	Date	N/A
e. Compiled financial forecast is presented on another comprehensive basis of accounting other than generally accepted accounting principles and it does not include disclosure of the basis used. [AAG-PRO 14.11]	______	______	☐
f. Prospective statements presented with historical statements. The report should also cover the historical financial statements. [AAG-PRO 14.06]	______	______	☐
16. For forecasts presented in tax shelter offerings, obtain a tax opinion that complies with U.S. Treasury Department Circular 230.	______	______	☐
17. Date the compilation report as of the date the compilation was completed. [AAG-PRO 14.04]	______	______	☐
18. Document any other procedures performed or unusual problems and their resolution.	______	______	☐
19. Determine that all required forms and checklists have been completed.	______	______	☐
20. Determine that all review points by the engagement team and the technical reviewer (if applicable) have been resolved.	______	______	☐

Prepared by: ______________________ Date: ______________
(In-Charge)

Reviewed by: ______________________ Date: ______________
(Partner)

13.905

Form for Presentation of Prospective Financial Statements

Client: ______________________

Prospective Financial Statement Date: ______________________

INSTRUCTIONS:

The following is a guide for the presentation of prospective financial statements and the accountant's report on the statements. References are to the AICPA *Guide for Prospective Financial Information.*

Preparer: ______________________ Date: ______________________

	Yes	No	N/A
PREPARATION OF PRESENTATION:			
1. Has the full legal name of the client been used or, if the entity has not been formed, has its name, form, and ownership interests been disclosed?	___	___	___
2. Do the titles of the statements adequately describe the nature of the presentation and the prospective period covered? [AAG-PRO 8.05]	___	___	___
3. Are all columns clearly labeled for comparative presentations? [AAG-PRO 8.44-.45]	___	___	___
4. For OCBOA presentations, do statement titles reflect the basis used?	___	___	___
5. When the forecast or projection is presented as a range, does the presentation explain that the range does not represent the best or worst possible results [AAG-PRO 8.21], and that while results are expected to fall within the range, there is no assurance they will? [AAG-PRO 8.30]	___	___	___
6. Is the period covered by the presentation appropriate? [AAG-PRO 8.32-.33]	___	___	___
a. Does the presentation cover at least one year's operations?	___	___	___
b. If a short period or interim period is presented, is such period consistent with the use of the presentation?	___	___	___

FORM FOR PRESENTATION OF PROSPECTIVE FINANCIAL STATEMENTS (Continued)

	Yes	No	N/A
c. When longterm results are meaningful to the presentation, have sufficient periods or an explanation of the results been included?	___	___	___
7. Does each page of the presentation contain a reference to the significant assumptions and accounting policies?	___	___	___
8. Prospective financial statements preferably should be in the format of the historical financial statements that would be issued for the period. [AAG-PRO 8.06]	___	___	___
a. Are the statements issued in the historical format?	___	___	___
b. If not, is there an agreement between the responsible party and potential users specifying another format?	___	___	___
c. If the presentation is limited, does it contain the minimum items required by Appendix A of Section 200 in Statements on Standards for Attestation Engagements No. 1, *Attestation Standards*. (AT 200.67)	___	___	___

ACCOUNTING PRINCIPLES AND POLICIES:

	Yes	No	N/A
1. a. Is the presentation prepared on the basis of principles expected to be used for historical statements during the prospective period for fore- casts, or	___	___	___
b. If the presentation is a projection and principles are different, is the use of different principles consistent with the purpose of the presentation and are disclosures adequate? [AAG-PRO 8.13 and 8.13P]	___	___	___
2. If the basis used in the presentation is not consistent with the basis expected to be used for historical statements, has a reconciliation or explanation of the differences been included in the presentation? [AAG-PRO 8.15]	___	___	___
3. Have any changes from principles used in prior-period historical statements been reported as would be required for historical statements? [AAG-PRO 8.16]	___	___	___
4. Have all significant accounting policies been disclosed? [AAG-PRO 8.12]	___	___	___
5. Has any OCBOA been described in the summary of accounting policies? [AAG-PRO 8.14]	___	___	___

ASSUMPTIONS:

FORM FOR PRESENTATION OF PROSPECTIVE FINANCIAL STATEMENTS (Continued)

	Yes	No	N/A
1. Has a summary of significant assumptions been presented? [AAG-PRO 8.22–.23 and 8.26]	___	___	___
2. Is the basis or rationale for the assumptions disclosed? [AAG-PRO 8.22]	___	___	___
3. Does the introduction to the summary of significant assumptions include the following:			
a. An indication of which assumptions are particularly sensitive? [AAG-PRO 8.24–.25]	___	___	___
b. A statement that assumptions disclosed are not all-inclusive and that they are based on the responsible party's current judgment? [AAG-PRO 8.28]	___	___	___
c. A description of the intent of the forecast or projection? [AAG-PRO 8.28]	___	___	___
d. A caveat that the prospective results may not be attained? [AAG-PRO 8.28]	___	___	___
e. The date of preparation of the presentation? [AAG-PRO 8.11]	___	___	___
f. For projections, an explanation of any special purpose and any limitations of usefulness. [AAG-PRO 8.29P]	___	___	___
g. For projections, any disclosure of hypothetical assumptions. Any improbable hypothetical assumptions should be identified. [AAG-PRO 8.29P]	___	___	___
h. A statement that the responsible party does not intend to update the presentation (optional).	___	___	___
i. If the presentation is a range, a statement that the responsible party expects the results to fall within the range although there can be no assurance that they will.	___	___	___

Prepared by: ______________________ Date: ______________
(In-Charge)

Reviewed by: ______________________ Date: ______________
(Partner)

3.906 Representation Letter — Compilation of Financial Forecast

[Client Letterhead]

[Date of Accountant's Report]

[To the Accountant]

In connection with your compilation of the forecasted balance sheet and the related forecasted statements of earnings, retained earnings and cash flows, and summaries of significant assumptions and accounting policies as of _____ [forecast date] and for the year then ending, we make the following representations:

1. The financial forecast presents our assumptions and, to the best of our knowledge and belief, the Company's expected financial position, results of operations, and cash flows in conformity with the generally accepted accounting principles* expected to be used by the Company during the forecast period, which are consistent with the principles the Company uses in preparing its historical financial statements.

2. The financial forecast is based on our judgment of the expected conditions and our expected course of action.

3. We have made available to you all significant information that we believe is relevant to the forecast.

4. We believe that the assumptions underlying the forecast are reasonable and appropriate.

5. To the best of our knowledge and belief, the documents and records supporting the assumptions are appropriate.

____
[Name of Owner or Chief Executive Officer and Title]

____
[Name of Chief Financial Officer and Title, where applicable]

* The representation letter should be modified when the financial statements are prepared in accordance with an other comprehensive basis of accounting.

13.907 Representation Letter — Compilation of Financial Projection

[Client Letterhead]

[Date of Accountant's Report]

[To the Accountant]

In connection with your compilation of the projected balance sheet and related statements of earnings, retained earnings and cash flows, and summaries of significant assumptions assuming ______________ [describe hypothetical assumptions] and accounting policies as of ____ [projection date] and for the year then ending, we make the following representations:

1. The financial projection presents our assumptions and, to the best of our knowledge and belief, the Company's expected financial position, results of operations, and cash flows for the projection period assuming ______________________________ [describe hypothetical assumptions].
2. The accounting principles used in the financial projection are in accordance with the generally accepted accounting principles

* expected to be used by the Company during the projection period, which are consistent with the principles the Company uses in preparing its historical financial statements. (If different principles are used, consider stating the principles are consistent with special purpose of projection.)

3. The financial projection is based on our judgment, considering present circumstances, of the expected conditions and our expected course of action assuming ________________________ [describe hypothetical assumptions].
4. We have made available to you all significant information that we believe is relevant to the financial projection.
5. We believe that the assumptions underlying the projection are appropriate and reasonable assuming ________________________ [describe hypothetical assumptions].
6. To the best of our knowledge and belief, the documents and records supporting the assumptions are appropriate.
7. We intend to use this projection only for [describe limited use].

____
[Name of Owner or Chief Executive Officer and Title]

____
[Name of Chief Financial Officer and Title, where applicable]

* This representation letter should be modified when the financial statements are prepared in accordance with an other comprehensive basis of accounting.

13.908 Compilation Report — Forecast

____

____

____

I (We) have compiled the accompanying forecasted balance sheet and the related forecasted statements of earnings, retained earnings, and cash flows of ____ [client name] as of __________________________________ [forecast date], and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of a forecast information that is the representation of management and does not include evaluation of the support for the assumptions underlying the forecast. I (We) have not examined the forecast and, accordingly, do not express an opinion or any other form of assurance on the accompanying statements or assumptions. Furthermore, there usually will be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. I (We) have no responsibility to update this report for events and circumstances occurring after the date of this report.

[Signature]

[Date]

____

Notes:

1. If the firm is not independent, add the following sentence as a separate paragraph:

   I (We) are not independent with respect to ________ [client name].

2. Summarized or minimum presentations should be appropriately described.

3. When the prospective financial statements are presented using a basis of accounting other than generally accepted accounting principles, the other basis must either be disclosed in the summary of significant accounting policies or in the compilation report. Statements also must be titled using terminology applicable to the other basis. The report might appear as follows:

   ...and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants. This financial forecast is presented on the accounting basis [describe basis], which is a comprehensive basis of accounting other than generally accepted accounting principles.

4. If management has elected to omit the summary of accounting policies, the following paragraph should be added to the compilation report:

   Management has elected to omit the summary of significant accounting policies required by the guidelines for presentation of a forecast established by the American Institute of Certified Public Accountants. If the omitted disclosures were included in the forecast, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows for the forecast period. Accordingly, this report is not designed for those who are not informed about such matters.

13.909 Compilation Report — Projection

____
____
____

I (We) have compiled the accompanying projected balance sheet and the related projected statements of earnings, retained earnings, and cash flows of ______________________ [client name] as of ____________________ [projection date], and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants.

The accompanying projection and this report were prepared for [state special purpose] and should not be used for any other purpose.

A compilation is limited to presenting in the form of a projection information that is the representation of management and does not include evaluation of the support for the assumptions underlying the projection. I (We) have not examined the projection and, accordingly, do not express an opinion or any other form of assurance on the accompanying statements or assumptions. Furthermore, even if ______________________ [Describe Hypothetical Assumption], there usually will be differences between the projected and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. I (We) have no responsibility to update this report for events and circumstances occurring after the date of this report.

[Signature]

[Date]

Notes:

1. If the firm is not independent, add the following sentence as a separate paragraph:

   I (We) are not independent with respect to ________ [client name].

2. Summarized or minimum presentations should be appropriately described.

3. When the prospective financial statements are presented using a basis of accounting other than generally accepted accounting principles, the other basis must either be disclosed in the summary of significant accounting policies or in the compilation report. Statements also must be titled using terminology applicable to the other basis. The report might appear as follows:

   ...and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants. This financial projection is presented on the accounting basis [Describe Basis], which is a comprehensive basis of accounting other than generally accepted accounting principles.

4. If management has elected to omit the summary of accounting policies, the following additional paragraph should be added to the compilation report:

   Management has elected to omit the summary of significant accounting policies required by the guidelines for presentation of a projection established by the American Institute of Certified Public Accountants. If the omitted disclosures were included in the projection, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows for the projection period. Accordingly, this report is not designed for those who are not informed about such matters.

13.910 Transmittal Letter — Plain Paper Engagements

This transmittal letter may be prepared for plain paper engagements. No report on the service should be included with the presentation.

Dear ____________________:

A presentation of __________________ [name of company] forecasted (projected) statement for the period ending _________________ is enclosed. It is intended for internal use of management only and should not be used for any other purpose. The actual results may vary from those presented and the variations may be material.

Sincerely,

____
[Partner's Name]

13.911 Assembly Report — Forecast

____
____
____

I (We) have assembled, from information provided by the management, the accompanying forecasted balance sheet and the related forecasted statements of earnings, retained earnings, and cash flows of ____ [client name] as of ______________________ [forecast date], and for the year then ending. [If applicable—This financial forecast omits the summary of significant accounting policies.] I (We) have not compiled or examined the financial forecast and express no assurance of any kind on it. Further, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. In accordance with the terms of our engagement, this report and the accompanying forecast are restricted to internal use and may not be shown to any third party for any purpose.

[Signature]

[Date]

Notes:

1. If the firm is not independent, add the following sentence as a separate paragraph:

   I (We) are not independent with respect to _________ [client name].

2. Partial presentations' reports should also contain explanations of any limitations on the usefulness of the presentation.

3. When the prospective financial statements are presented using a basis of accounting other than generally accepted accounting principles, the other basis must either be disclosed in the summary of significant accounting policies, or in the assembly report. Statements also must be titled using terminology applicable to the other basis. Insert the following sentence when report disclosure is required:

   This financial forecast is presented on the __________ basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles.

13.912 Assembly Report — Projection

____
____
____

I (We) have assembled, from information provided by the management, the accompanying projected balance sheet and the related projected statements of earnings, retained earnings, and cash flows of ________________________ [client name] as of ________________ [projection date], and for the year then ending. [If applicable—This financial projection omits the summary of significant accounting policies.] The accompanying projection and this report were prepared for [State Special Purpose] and should not be use for any other purpose. I (We) have not compiled or examined the financial projection and express no assurance of any kind on it. Further, even if ________________________ [describe hypothetical assumptions], there will usually be differences between the projected and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. In accordance with the terms of our engagement, this report and the accompanying projection are restricted to internal use and may not be shown to any third party for any purpose.

[Signature]

[Date]

Notes:

1. If the firm is not independent, add the following sentence as a separate paragraph:

   I (We) are not independent with respect to ________ [client name].

2. Partial presentations' reports should also contain explanations of any limitations on the usefulness of the presentation.

3. When the prospective financial statements are presented using a basis of accounting other than generally accepted accounting principles, the other basis must either be disclosed in the summary of significant accounting policies, or in the assembly report. Statements must also be titled using terminology applicable to the other basis. Insert the following sentence when report disclosure is required:

   This financial projection is presented on the __________ basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles.

Illustrative
Financial Statements
and Disclosures

CHAPTER 14

ADDITIONAL ILLUSTRATIVE FINANCIAL STATEMENTS AND DISCLOSURES

14.000 INTRODUCTION

14.001 This chapter describes selected financial statement disclosures and provides additional illustrative financial statements for certain specialized entities. It also includes a financial statement disclosure checklist for full disclosure compilation and review engagements.

14.100 SELECTED FINANCIAL STATEMENT DISCLOSURES

14.101 This section of the chapter provides a description of selected financial statement disclosures, including illustrative notes to the financial statements.

Accounting Changes and Corrections of Errors

14.102 Accounting Principles Board (APB) No. 20, *Accounting Changes*, describes the accounting and disclosure requirements for a change in accounting estimate, a change in accounting principle, and a correction of an error in prior-period financial statements.

14.103 A change in accounting estimate should be accounted for prospectively — that is, by using the new estimate in the current and future periods (unless the change in estimate is inseparable from a change in principle). The effects on income before extraordinary items and net income of the current period should be disclosed if the change in estimate affects several future periods, such as a change in the useful lives of depreciable assets. Disclosure of the effect of the change is not necessary for estimates made each period in the ordinary course of accounting for items, such as estimates of uncollectible accounts.

14.104 Changes in accounting principle generally are accounted for by presenting the cumulative effect of the change on prior periods (net of applicable income taxes) as a separate item in the current income statement between the captions *extraordinary items* and *net income*. Financial statements for prior periods included for comparative purposes should be presented as previously reported, but the pro-forma effects of retroactive application of the new accounting principle on income before extraordinary items and net income for that period should be shown on the face of the income statement (if the amounts can be determined). In addition, a note to the financial statements should disclose the nature of and justification for the change, and the effects of adopting the new accounting principle on income before extraordinary items and on net income of the current period.

14.105 Certain changes in accounting principle are accounted for by retroactive restatement of prior periods. These include: (a) a change from the last-in, first-out (LIFO) method of inventory pricing to another method, (b) a change in the method of accounting for long-term construction-type contracts, (c) a change to or from the full cost method of accounting that is used in the extractive industries, and (d) a change from retirement-replacement-betterment accounting to depreciation accounting. In addition to the nature of and justification for the change, the financial statements should disclose the effects of applying the new principle on income before extraordinary items and net income for all periods presented.

14.106 Errors in financial statements result from mathematical mistakes, mistakes in the application of accounting principles, or oversight of facts that existed at the time the financial statements were issued. The nature of the error and the effects of its correction on income before extraordinary items and net income of any comparative financial statements presented should be disclosed. If financial statements for only the current period are presented, this disclosure should indicate the effects of the restatement on the beginning balance of retained earnings and on net income of the immediately preceding period.

Change from OCBOA to GAAP or Vice Versa

14.107 A change from an other comprehensive basis of accounting (OCBOA) presentation, such as from the income tax basis of accounting, to the accrual basis of accounting or vice versa, should be treated as a prior period adjustment in accordance with FASB Statement No. 16, *Prior Period Adjustments*. Previously-issued financial statements should be restated if those statements are presented with the financial statements of the current period. If only the current-period statements are presented, the adjustments should be reflected in the opening balance of retained earnings.

14.108 Disclosure should be made in the notes to the financial statements of the period in which the change in accounting basis is made. The nature of the change in previously issued financial statements and its effect on net income should be described. If the change is disclosed, the accountant need not modify the standard compilation or review report to emphasize the matter; however, he or she is not precluded from doing so. (See Technical Practice Aid [TPA] 9210.10 and TPA 9210.11, reproduced in Appendix B.)

14.109 Illustrative Disclosures of Accounting Changes and Corrections of Errors

Change in Accounting Estimate

Note 4 — Change in Accounting Estimate

At the beginning of 19X2, the Company decreased the estimated remaining useful lives of its computer equipment based on technological changes. Remaining lives which averaged four years were decreased to two years. The effect of this change in accounting estimate was to decrease net income by $15,000.

Change in the Basis of Accounting

Note 2 — Change in the Basis of Accounting

Effective January 1, 19X1, the Company changed the basis of accounting for its financial statements from the method used for federal income tax purposes to generally accepted accounting principles. The effect of this change in the basis of accounting was to increase net income for 19X1 by $23,500.

Inventories

Note 4 — Change in Accounting for Inventories

In 19X4, the Company changed its method of accounting for inventories from the first-in, first-out (FIFO) method to the last-in, first-out (LIFO) method. Management believes that the change is to a preferable method because the LIFO method will more clearly match current costs with current revenues. There is no cumulative effect on retained earnings as of January 1, 19X4 from adopting LIFO, and pro-forma amounts from retroactive application are not presented because they are not determinable. The effect of this change for 19X4 was to decrease net income for the year by $123,000.

Income Taxes

Note 5 — Change in Accounting for Income Taxes

Effective January 1, 19X3, the Company adopted FASB Statement No. 109, *Accounting for Income Taxes*. The change had the effect of reducing 19X3 net earnings by $56,000, including $43,000 for the cumulative effect on years prior to 19X3.

Correction of an Error

Note 3 — Correction of Error

The financial statements for 19X3 have been restated to correct a $35,000 mathematical error in computing inventory at December 31, 19X3. Correction of the error has the effect of reducing net earnings as originally reported by $12,300.

Significant Concentrations of Credit Risk

14.110 FASB Statement No. 105, *Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk*, requires disclosure of certain information about significant concentrations of credit risk arising for all types of financial instruments, including accounts receivable. These disclosures include:

- Information about the activity, region, or economic characteristics that identifies the concentration.
- The amount of accounting loss due to credit risk the entity would incur if the parties to the financial instruments failed to perform in accordance with the terms of the agreements, and the collateral, if any, proved to be of no value.
- The entity's policy of requiring collateral or other security to support the financial instruments subject to credit risk, a description of the collateral or other security, and information about the entity's access to it.

Often the concentration of credit risk is obvious from a description of the entity's business. In that case, no additional disclosure is necessary.

14.111 Illustrative Disclosures of Concentrations of Credit Risk

Note 1 — Nature of the Business

The Company is a retail family clothing store located in Paris, Texas. The Company grants credit to customers, substantially all of whom are local residents.

Note 4 — Concentration of Credit Risk

A significant portion of the Company's customers are small retailers of electronics in the southern region of New Jersey. At December 31, 19X9, the net balance of accounts receivable from these customers was $237,000.

Note 5 — Concentrations of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of temporary cash investments and trade receivables. The Company places its temporary cash investments with high credit quality financial institutions and, by policy, limits the amount of credit exposure to any one financial institution to the amount of Federal Deposit Insurance Corporation (FDIC) coverage. Concentrations of credit risk with respect to trade receivables are limited due to the large number of customers comprising the Company's customer base. As of December 31, 19X8, the Company had no significant concentrations of credit risk.

Practice Tip:

If the entity has a significant uninsured cash balance with a single bank, disclosure of that fact generally should be made because it is a significant credit risk. In contrast, numerous immaterial uninsured cash balances on deposit with several banks may not require disclosure. The threshold for "significance" will vary with individual circumstances and is a matter of judgment.

Related-Party Transactions

14.112 FASB Statement No. 57, *Related Party Disclosures*, specifies the disclosure required for material related-party transactions, including —

- The nature of the relationship(s).
- A description of the transactions, including transactions to which no amounts or nominal amounts were ascribed, for each of the periods for which an income statement is presented.
- The dollar amounts of transactions for each of the periods for which income statements are presented and the effects of any change in the method of establishing the terms from that used in the preceding period.

- Amounts due from or to related parties as of the date of each balance sheet presented and, if not otherwise apparent, the terms and manner of settlement.

Practice Tip:

An entity may be economically dependent on a major customer. Although the requirement to disclose information about sales to major customers was suspended for nonpublic entities by FASB Statement No. 21, *Suspension of Reporting of Earnings per Share and Segment Information by Nonpublic Enterprises*, the suspension does not affect the requirement for such entities to disclose information about economic dependency when such disclosure may be necessary for a fair presentation. FASB Statement No. 57, *Related Party Disclosures*, requires disclosure of material transactions with "parties with which the entity may deal if one party...can significantly influence the operating policies of the other to the extent that one of the transacting parties might be prevented from fully pursuing its own separate interests." Furthermore, SOP 94-6, *Disclosure of Certain Significant Risks and Uncertainties*, requires disclosure of certain significant concentrations. Financial statement preparers should consider the circumstances in each engagement to determine whether such disclosure is necessary for a fair presentation.

14.113 Illustrative Disclosures of Related-Party Transactions

Purchase of Property

Note 5 — Related-Party Transaction

In June 19X7, the Company purchased real property adjoining its location from the Company's president for $250,000.

Lease

Note 6 — Transactions with Related Parties

The Company leases its office building from a partnership that is owned by two stockholders of the Company on a month-to-month basis. The total amount of the lease payments for 19X1 was $56,000. At December 31, 19X1, the Company owed the partnership $4,300.

Legal Services

Note 6 — Related-Party Transactions

Mr. Toole, a director and officer of the Company, is a partner in the law firm of Wilson and Watson. The statements of income for 19X1 and 19X0 include $34,000 and $26,000, respectively, for legal services rendered by Wilson and Watson. Accounts payable at December 31, 19X1 include $10,000 payable to Wilson and Watson.

Contingencies

14.114 FASB Statement No. 5, *Accounting for Contingencies*, states that loss contingencies should be accrued in the financial statements if it is *probable* that a loss has occurred and the loss can be *reasonably estimated*. Loss contingencies should be disclosed in the financial statements if it is at least *reasonably possible* that a loss has occurred. Contingencies that are *remote* need not be disclosed unless disclosure is traditional, for example, disclosure of guarantees of indebtedness of others, obligations of commercial banks under standby letters of credit, and guarantees to repurchase receivables that have been sold. If the contingency is accrued, disclosure should include the nature of the contingency and an estimate of any additional amount of loss that is reasonably possible, or a statement that such an estimate cannot be made. Disclosure of a loss contingency that has not been accrued should include—

- The nature of the contingency, and
- An estimate of the possible loss or range of loss or a statement that such an estimate cannot be made.

14.115 Gain contingencies should be adequately disclosed, but care should be exercised to avoid misleading implications as to the likelihood of realization.

14.116 Illustrative Disclosures of Contingencies

Litigation

Note 7 — Litigation

The Company is a defendant in a lawsuit alleging breach of a lease agreement, in which the plaintiff is seeking to recover damages of approximately $300,000. The case is currently in arbitration and the ultimate outcome of the dispute cannot be determined at this time. The Company's legal counsel believes that the claim is without substantial merit and the eventual liability, if any, will not be material to the financial position of the Company.

Guarantees of Indebtedness of Others

Note 7 — Contingent Liabilities

The Company has guaranteed the indebtedness of $500,000 borrowed by the president and principal stockholder of the Company.

Note 8 — Contingencies

The Company is contingently liable for $700,000 related to guarantees of indebtedness of an affiliated company.

Possible Tax Assessment

Note 6 — Contingencies

During 19X8, the Internal Revenue Service (IRS) completed an examination of the Company's federal income tax returns for 19X3 through 19X5. The IRS disagrees with the Company's practice of excluding certain dividends received from taxable income and has advised it will propose assessments of approximately $600,000. The Company believes that its position is fully supported and will vigorously oppose the assessments. In the opinion of management the ultimate resolution of this issue will have no material adverse financial effect.

Uncertainties About Going-Concern

14.117 Significant uncertainties about an entity's ability to continue as a going concern should be disclosed in the notes to the financial statements. According to Statements on Auditing Standards (SAS) No. 59, *The Auditor's Consideration of an Entity's Ability to Continue as a Going-Concern,* information that might be disclosed includes:

- Pertinent conditions and events giving rise to substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time (i.e., one year from the balance-sheet date).
- The possible effects of such conditions and events.
- Management's evaluation of the significance of those conditions and events and any mitigating factors.
- Management's plans.
- Information about the recoverability or classification of recorded asset amounts or the amounts or classification of liabilities.

14.118 Illustrative Disclosures of Uncertainties About Going-Concern

Note 7 — Liquidity

For three consecutive years, the Company has incurred significant operating losses. At December 31, 19X5, the Company's current liabilities exceeded its current assets by $210,000. To obtain additional financing, management has implemented a plan to obtain a loan from the Company's shareholders. The ability of the Company to continue as a going concern depends on the success of this plan which cannot be predicted at this time. The financial statements do not include any adjustments to assets or liabilities that might be necessary if the Company is unable to continue as a going concern.

14.200 ACCOUNTING AND DISCLOSURES FOR SPECIALIZED ENTITIES

14.201 Sections 14.300 through 14.500 of this chapter contain illustrative disclosures and financial statements for several specialized entities, including common interest realty associations, S Corporations, and development stage enterprises.

14.300 COMMON INTEREST REALTY ASSOCIATIONS

14.301 An accountant may be engaged to compile or review the financial statements of a common interest realty association. Common interest realty association (CIRA) is a term used to describe an association of owners that is responsible for providing certain services and maintaining certain property that all the owners share or own in common. Examples of CIRAs include homeowners' associations and condominium associations.

14.302 The main characteristics of the ownership of assets by CIRAs include the following:

- Individual ownership of a lot, defined interior space, or shares of stock
- Ownership through an association of owners of an undivided interest in the common property
- Automatic membership in a CIRA that has been established under state laws and that performs maintenance and other service activities for the owners
- Funding of the CIRA's activities by periodic assessments of the owners

14.303 A CIRA's function is to operate, preserve, maintain, repair, and replace common property and provide other services to the owners. Accordingly, CIRAs conduct and report on two primary kinds of activities —

- Normal maintenance and service operations, such as gardening, management, snow removal, minor repairs, and janitorial services
- Long-term major repair and replacement requirements, such as roof replacements, street resurfacing, and painting

Method of Accounting

14.304 Generally accepted accounting principles for CIRAs, as set forth in the AICPA Audit and Accounting Guide, *Audits of Common Interest Realty Associations* (the CIRA guide), provides for the use of the accrual basis of accounting. If a CIRA prefers to use the cash basis of accounting, and the amounts differ materially from the accrual basis, the accountant should consider the financial statements to be presented on an other comprehensive basis of accounting. (See Chapter 9 for a discussion of financial statements prepared on an other comprehensive basis of accounting.)

14.305 The CIRA guide recommends use of fund reporting, which is commonly used by not-for-profit organizations. Nonfund reporting is an acceptable alternative, but not preferable, because it often does not disclose whether assessments were used for designated purposes.

Financial Statements

14.306 Full disclosure financial statements of a CIRA that are presented in conformity with generally accepted accounting principles (GAAP) should include the following:

- A balance sheet

- A statement of revenues and expenses
- A statement of changes in fund balances (often combined with the statement of revenues and expenses)
- A statement of cash flows
- Notes to the financial statements

Required Supplementary Information

14.307 The CIRA guide establishes a unique requirement for financial statements of CIRAs — required supplementary information. This information, which is not considered to be part of the basic financial statements, includes:

- Estimates of current or future costs of future major repairs and replacements of all existing components of common property, with disclosure of the methods used to determine the costs, the basis for calculations, sources used, and the dates of any studies made for this purpose.
- A presentation of components to be repaired and replaced, estimates of the remaining useful lives of those components, estimates of current or future replacement costs, and amounts of funds accumulated for each to the extent designated by the CIRA's board of directors. (An illustration of this required supplementary information is included with the illustrative financial statements in this chapter.)

14.308 There is no requirement for CIRAs to obtain studies prepared by professional engineers to prepare this supplementary information. The information may be prepared by the CIRA's board of directors based on studies prepared by engineers, contractors, or suppliers, or by using tables in technical manuals on useful lives of components.

14.309 Paragraph 43 of SSARS No. 1, *Compilation and Review of Financial Statements*, states that when basic financial statements are accompanied by supplementary information, the accountant should clearly indicate the degree of responsibility, if any, he or she is taking with respect to the supplementary information. That requirement applies when the financial statements are accompanied by information *voluntarily* presented for supplementary analysis purposes; however, SSARSs do not address the accountant's responsibility when the financial statements are accompanied by *required* supplementary information. This created a reporting dilemma for the AICPA Accounting and Review Services Committee.

14.310 To resolve that problem, the AICPA issued Statement of Position (SOP) 93-5, *Reporting on Required Supplementary Information Accompanying Compiled or Reviewed Financial Statements of Common Interest Realty Associations*, to provide performance and reporting guidance when required supplementary information accompanies the basic financial statements in a compilation or review engagement. SOP 93-5 requires accountants to at least compile required CIRA supplementary information and indicate in the compilation or review report on the basic financial statements, or in a separate report, the degree of responsibility he or she is taking for the supplementary information. This precludes the accountant from taking no responsibility for the required CIRA supplementary information.

14.311 To compile the required supplementary information, the accountant should:

- Establish an understanding with the entity regarding the services the accountant will perform with respect to the required supplementary information and how that information will affect the report the accountant expects to render.
- Consider what supplementary information is required by the CIRA guide and how that information is to be presented.
- Obtain an understanding of how the required supplementary information was developed. This understanding ordinarily includes —
    - The source of the information (e.g., engineering reports, estimates obtained from contractors, tables in technical manuals on useful lives).
    - Whether the required supplementary information is based on current or future replacement costs.
    - The interest and inflation rates used to determine funding requirements if the information is based on future replacement costs.
- Consider whether it will be necessary to perform other accounting services to compile the required supplementary information.
- Read the required supplementary information and consider whether it appears to be appropriate in form and free from obvious material error.
- If the accountant becomes aware that the required supplementary information is incorrect, incomplete, or otherwise unsatisfactory, obtain additional or revised information.
- If the entity is unable or refuses to provide additional or revised information, consider whether a modification of the standard report is adequate to disclose the deficiency in the measurement or presentation of the required supplementary information. If modification of the standard report is not adequate to disclose the deficiency, withdraw from the engagement. If modification of the standard report is adequate to disclose the deficiency, the sentence illustrated in section 14.319 below should be added to the accountant's report.

14.312 In an engagement to review the basic financial statements, the required supplementary information is not subjected to the inquiry and analytical procedures applied to the review of the basic statements because the information is not derived from the entity's books and records; therefore, SSARSs do not apply to the review of this information. If the accountant is engaged to review the required supplementary information, he or she may do so in accordance with the Statement on Standards for Attestation Engagements No. 1, *Attestation Standards*.

Practice Tip:

Because of the subjective nature of the required supplementary information for CIRAs, the authors do not recommend that you accept an engagement to review this information.

14.313 When the accountant has compiled both the basic financial statements and the required supplementary information, the accountant should indicate, in an additional paragraph of the report or in a separate report, the degree of responsibility he or she is taking for the supplementary information. An example of an additional paragraph that may be added to the accountant's compilation report on the basic financial statements follows:

> The [identify the supplementary information] on page XX is not a required part of the basic financial statements but is supplementary information required by the American Institute of Certified Public Accountants. I (We) have compiled [identify the supplementary information] from information that is the representation of management of XYZ Association, without audit or review. Accordingly, I (we) do not express an opinion or any other form of assurance on the supplementary information.

An example of a complete report is provided in section 14.322 of this chapter.

14.314 When the accountant has reviewed the financial statements and compiled the required supplementary information, the accountant should report on the information in an additional paragraph of the report or in a separate report. An example of an additional paragraph that may be added to the review report on the basic financial statements follows:

> The [identify the supplementary information] on page XX is not a required part of the basic financial statements but is supplementary information required by the American Institute of Certified Public Accountants. The information has not been subjected to the inquiry and analytical procedures applied in the review of the basic financial statements, but was compiled from information that is the representation of XYZ Association, without audit or review. Accordingly, I (we) do not express an opinion or any other form of assurance on the supplementary information.

An example of a complete report is provided in section 14.323 of this chapter.

14.315 The CIRA guide includes several limited procedures that should be applied to the required supplementary information when the financial statements are audited. However, an accountant that has been engaged to compile or review a CIRA's financial statements also may be engaged to apply these limited procedures. Specifically, they include:

- Determine by physical inspection of the property or review of the CIRA's legal documents whether the disclosure includes all major property components.

- Compare estimates of the costs of major repairs and replacements with current period expenditures and with the annual budget, if any.
- Inquire of management about whether the CIRA's property maintenance records, which reflect each component's replacement history, if any, were considered in determining the information to be disclosed.
- Inquire of management about whether the age and condition of the components were considered in determining the information and amounts to be disclosed.
- Check the mathematical accuracy of amounts disclosed.
- Inquire of management about whether the study was prepared by the board or by a professional engineer and whether the methods and bases for estimating the amounts disclosed are documented. Consider whether those methods and bases are reasonable. If the study was conducted by the board, consider whether the source of the information used to estimate the useful lives and current or future repair and replacement costs (e.g., bids from contractors or technical manuals on useful lives of various components) are reasonable.

14.316 When the accountant has performed these limited procedures, a paragraph such as the following may be added to the accountant's review report.

> The [identify the supplementary information] on page XX is not a required part of the basic financial statements but is supplementary information required by the American Institute of Certified Public Accountants. We have applied certain limited procedures, which principally consisted of inquiries of management regarding the methods of measurement and presentation of the supplementary information. I (We) did not audit or review the supplementary information and, accordingly, do not express an opinion or any other form of assurance on it.

Omission of the Required Supplementary Information

14.317 If financial statements of a CIRA are not accompanied by the required supplementary information, a paragraph should be added to the accountant's report indicating that the required supplementary information has been omitted. The accountant need not present the supplementary information in the accountant's report. An example of an appropriately worded paragraph follows:

> The Association has not presented the required supplementary information about future major repairs and replacement costs of common property which the American Institute of Certified Public Accountants has determined is required to supplement, although not required to be a part of, the basic financial statements.

14.318 If the financial statements of the CIRA omit substantially all disclosures required by GAAP and the required supplementary information, the accountant should add the above paragraph in addition to the standard paragraph indicating the management has elected to omit substantially all disclosures required by GAAP.

Reporting When the Supplementary Information Departs from the Prescribed Guidelines

14.319 If, on the basis of information that comes to the accountant's attention, he or she concludes that the required supplementary information has not been measured or presented within prescribed guidelines, the accountant should suggest that the information be revised. If the client fails to revise the information, the accountant should consider whether modification of the standard report is adequate to disclose the deficiency. If modification of the standard report is considered adequate, the accountant should indicate in his or her compilation or review report that the information does not conform with the guidelines, and should describe the nature of any material departure(s). An example of a sentence that might be used in these circumstances follows:

> However, I (we) did become aware that the supplementary information about future major repairs and replacements is not presented in conformity with the guidelines established by the American Institute of Certified Public Accountants because [describe the material departure(s) from the AICPA guidelines].

If modification of the standard report is not adequate to disclose the deficiency, the accountant should withdraw from the engagement.

Illustrative Financial Statements and Accountant's Reports

14.320 The pages that follow contain illustrative financial statements for a condominium association and illustrative compilation and review reports.

14.321 Illustrative Financial Statements for a Common Interest Realty Association

Mirage Condominium Association, Inc.
Balance Sheet
as of December 31, 19X2
(with Comparative Totals for 19X1)

	19X2			19X1
	Operating Fund	Replacement Fund	Total	Total
ASSETS				
Cash and cash equivalents	$ 110,000	$ 364,000	$ 474,000	$ 298,000
Assessments receivable	28,000		28,000	9,000
Prepaid expenses	7,000		7,000	7,000
Due from operating fund		20,000	20,000	
Due to replacement fund	(20,000)		(20,000)	
Equipment, net of accumulated depreciation of $8,000 and $5,000	21,000		21,000	17,000
Total Assets	$ 146,000	$ 384,000	$ 530,000	$ 331,000
LIABILITIES				
Accounts payable	$ 20,000	$ 4,000	$ 24,000	$ 6,000
Wages payable	6,000		6,000	
Income taxes payable		1,000	1,000	5,000
Prepaid assessments	20,000		20,000	15,000
	46,000	5,000	51,000	26,000
FUND BALANCES	100,000	379,000	479,000	305,000
TOTAL LIABILITIES AND FUND BALANCES	$ 146,000	$ 384,000	$ 530,000	$ 331,000

See the accompanying notes and accountants' report.

Mirage Condominium Association, Inc.
Statements of Revenues and Expenses
and Changes in Fund Balances
for the Year Ended December 31, 19X2
(with Comparative Totals for 19X1)

	19X2			19X1
	Operating Fund	Replacement Fund	Total	Total
REVENUES				
Member assessments	$747,000	$ 247,000	$ 994,000	$ 909,000
Interest		49,000	49,000	46,000
Lawsuit settlements		141,000	141,000	91,000
Other	22,000		22,000	20,000
Total Revenues	769,000	437,000	1,206,000	1,066,000
EXPENSES				
Wages and benefits	294,000		294,000	284,000
Utilities	160,000		160,000	141,000
Roofs		144,000	144,000	160,000
Service and contracts	129,000		129,000	134,000
Exterior siding		94,000	94,000	98,000
Repairs and supplies	92,000		92,000	61,000
Insurance and licenses	50,000		50,000	46,000
Administrative	28,000		28,000	18,000
Income taxes	1,000	11,000	12,000	13,000
Legal fees		10,000	10,000	
Recreational equipment		5,000	5,000	2,000
Solar equipment		5,000	5,000	
Streets		4,000	4,000	20,000
Tennis courts				12,000
Depreciation	3,000		3,000	3,000
Bad debts	2,000		2,000	
Pools and spas				18,000
Total Expenses	759,000	273,000	1,032,000	1,010,000
Excess of revenues over expenses	10,000	164,000	174,000	56,000
Beginning fund balances	80,000	225,000	305,000	249,000
Transfer from replacement fund	10,000	(10,000)		
ENDING FUND BALANCES	$100,000	$ 379,000	$ 479,000	$ 305,000

See the accompanying notes and accountants' report.

Mirage Condominium Association, Inc.
Statements of Cash Flows
for the Year Ended December 31, 19X2
(with Comparative Totals for 19X1)

	19X2			19X1
	Operating Fund	Replacement Fund	Total	Total
Excess of revenues over expenses	$ 10,000	$ 164,000	$ 174,000	$ 56,000
Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities:				
Increase (decrease) in interfund balances	20,000	(20,000)		
Transfer from replacement fund	10,000	(10,000)		
Depreciation	3,000		3,000	3,000
Increase in assessments receivable	(19,000)		(19,000)	(1,000)
Decrease in prepaid expenses				1,000
Increase in accounts payable	14,000	4,000	18,000	2,000
Increase in wages payable	6,000		6,000	
Decrease in income taxes payable		(4,000)	(4,000)	
Increase in prepaid assessments	5,000		5,000	7,000
Total adjustments	39,000	(30,000)	9,000	12,000
Net cash provided by operating activities	49,000	134,000	183,000	68,000
Cash flows from investing activities:				
Equipment purchases	(7,000)		(7,000)	(3,000)
Net increase in cash and cash equivalents	42,000	134,000	176,000	65,000
Cash and cash equivalents at beginning of year	68,000	230,000	298,000	233,000
Cash and cash equivalents at end of year	$ 110,000	$ 364,000	$ 474,000	$ 298,000

See the accompanying notes and accountants' report.

Mirage Condominium Association, Inc.
Notes to Financial Statements

Note 1 — Organization

The Mirage Condominium Association is a statutory condominium association organized as a not-for-profit corporation for the purposes of maintaining and preserving common property of the Mirage condominium. The Mirage condominium consists of 300 residential units occupying a site of approximately 10 acres in Southwest U.S.A. The Association began its operations in June, 19XX.

Note 2 — Summary of Significant Accounting Policies

Fund accounting. The Association uses fund accounting, which requires that funds, such as operating funds and funds designated for future major repairs and replacements, be classified separately for accounting and reporting purposes. Disbursements from the operating fund are generally at the discretion of the board of directors and property manager. Disbursements from the replacement fund generally may be made only for designated purposes.

Interest earned. The board's policy is to allocate to the replacement fund interest earned on all cash accounts net of income taxes.

Recognition of assets and depreciation policy. The Association recognizes personal property assets at cost. The property is depreciated over its estimated useful life using the straight-line method of depreciation.

Use of estimates. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note 3 — Owners' Assessments

Monthly assessments to owners were $103.54 and $94.69 in 19X2 and 19X1. Of those amounts, $25.73 and $22.50 were designated to the replacement fund.

The annual budget and assessments of owners are determined by the board of directors and are approved by the owners. The Association retains excess operating funds at the end of the operating year, if any, for use in future operating periods.

Note 4 — Future Major Repairs and Replacements

The Association's governing documents require that funds be accumulated for future major repairs and replacements. Accumulated funds are held in separate savings accounts and generally are not available for expenditures for normal operations.

The board of directors conducted a study in November 19X2 to estimate the remaining useful lives and the replacement costs of the components of common property. The estimates were obtained from licensed contractors who inspected the property. The table included in the unaudited supplementary information on Future Major Repairs and Replacements is based on the study.

The board is funding for major repairs and replacements over the remaining useful lives of the components based on the study's estimates of current replacement costs and considering amounts previously accumulated in the replacement fund. Accordingly, the funding requirement of $302,000 has been included in the 19X3 budget.

Funds are being accumulated in the replacement fund based on estimates of future needs for repairs and replacements of common property components. Actual expenditures may vary from the estimated future expenditures, and the variations may be material. Therefore, amounts accumulated in the replacement fund may not be adequate to meet all future needs for major repairs and replacements. If additional funds are needed, the Association has the right, subject to membership approval, to increase regular assessments, pass special assessments, or delay major repairs and replacements until funds are available.

The Association used $30,000 from the replacement fund for operations during 19X2. The board intends to repay $20,000 of that amount during 19X3 and has, therefore, reflected $20,000 as an interfund receivable and payable. The board does not intend to repay $10,000 of the amount and has, therefore, reflected $10,000 as a transfer from the replacement to the operating fund.

Note 5 — Federal and State Taxes

In 19X2, the Association filed its income tax return as a regular corporation. The Association had an excess of expenses for the maintenance of the common property over membership source income. That excess may be carried over to future periods to offset future income from membership sources when the Association files as a regular corporation. In 19X1, the Association elected to file as a homeowners' association in accordance with Internal Revenue Service Code section 528. Under that section, the Association excludes from taxation exempt function income, which generally consists of revenue from uniform assessments to owners. In both years, the Association's investment income and other nonexempt income were subject to tax.

Note 6 — Lawsuit Settlements

During 19X1, the Association settled a lawsuit against the developer for defective construction and received a partial settlement of $91,000. During 19X2, the Association received another settlement of $141,000. Legal fees of $10,000 were incurred in connection with that lawsuit.

The following net amounts have been added to the replacement fund:

	19X2	19X1
Roof	$131,000	$66,000
Tennis courts	0	23,000
Pools and spas	0	1,000
Streets	0	1,000
TOTAL	$131,000	$91,000

Note 7 — Assessments Receivable

The Association's policy is to retain legal counsel and place liens on the properties of homeowners whose assessments are thirty days in arrears. As of December 31, 19X2, the Association had assessments receivable of $28,000, of which $22,000 were delinquent. As of February 23, 19X3, judgments and settlements of approximately $15,000 have been received. It is the opinion of the board of directors that the Association will ultimately prevail against the remaining homeowners whose assessments are delinquent and, accordingly, no allowance for uncollectible accounts is deemed necessary.

Mirage Condominium Association, Inc.
Supplementary Information on Future Major Repairs and Replacements
December 31, 19X2

The board of directors conducted a study in November 19X2 to estimate the remaining useful lives and the replacement costs of the components of common property. The estimates were obtained from licensed contractors who inspected the property.

The following table is based on the study and presents significant information about the components of common property.

Components	Estimated Remaining Useful Lives (Years)	Estimated Current Replacement Costs	19X3 Funding Requirement	Components of Fund Balance at Dec. 31, 19X2
Roofs	5 to 14	$1,620,000	$120,000	$154,000
Streets	5 to 14	96,000	40,000	57,000
Recreation facilities	2 to 11	120,000	12,000	55,000
Exterior siding	7 to 11	760,000	72,000	48,000
Pools, spas, solar equipment	2 to 14	112,000	36,000	39,000
Tennis courts	5 to 10	64,000	10,000	14,000
Furniture and equipment	3 to 7	80,000	12,000	12,000
		$2,852,000	$302,000	$379,000

See accountants' report.

14.322 Illustrative Compilation Report — Common Interest Realty Association

The Board of Directors
Mirage Condominium Association, Inc.
Los Angeles, California

We have compiled the accompanying balance sheets of Mirage Condominium Association, Inc. as of December 31, 19X2 and 19X1, and the related statements of revenues and expenses and changes in fund balances, and statements of cash flows for the years then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements and supplementary schedules information that is the representation of management. We have not audited or reviewed the accompanying financial statements and supplementary information and, accordingly, do not express an opinion or any other form of assurance on them.

The Supplementary Information on Future Major Repairs and Replacements on page X is not a required part of the basic financial statements but is supplementary information required by the American Institute of Certified Public Accountants. We have compiled the Supplementary Information on Future Major Repairs and Replacements from information that is the representation of Mirage Condominium Association, Inc., without audit or review. Accordingly, we do not express an opinion or any other form of assurance on the supplementary information.

Warren & Wood, CPAs
Los Angeles, California

February 12, 19X3

14.323 Illustrative Review Report — Common Interest Realty Association

The Board of Directors
Mirage Condominium Association, Inc.
Los Angeles, California

We have reviewed the accompanying balance sheets of Mirage Condominium Association, Inc. as of December 31, 19X2 and 19X1, and the related statements of revenues and expenses and changes in fund balances, and statements of cash flows for the years then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management of Mirage Condominium Association, Inc.

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

The Supplementary Information on Future Major Repairs and Replacements on page X is not a required part of the basic financial statements but is supplementary information required by the American Institute of Certified Public Accountants. The information has not been subjected to the inquiry and analytical procedures applied in the review of the basic financial statements, but was compiled from information that is the representation of Mirage Condominium Association, Inc., without audit or review. Accordingly, we do not express an opinion or any other form of assurance on the supplementary information.

Warren & Wood, CPAs
Los Angeles, California

February 12, 19X3

14.400 S CORPORATIONS

14.401 Generally accepted accounting principles for S Corporations are substantially the same as those for regular corporations; but there are certain differences. This section focuses on those differences.

Financial Statements of S Corporations

14.402 The basic financial statements of an S Corporation are the same as those for a regular corporation. If the financial statements of an S Corporation are presented in accordance with GAAP, they should include the following:

- The balance sheet
- The statement of income
- The statement of cash flows

14.403 An S Corporation's retained earnings account generally consists of various components, such as preelection accumulations, shareholders' undistributed taxable income previously taxed, an accumulated adjustment account, and other adjustment accounts. However, an AICPA Technical Practice Aid (TPA 7910.03) indicates that retained earnings of an S Corporation should be shown as a single balance sheet caption and amount. The components of retained earnings may be disclosed in the notes to the financial statements or supplementary information if it is meaningful to users of the financial statements.

Unique Disclosures of S Corporations

14.404 Disclosures that are unique to S Corporations include the following:

- The fact that the corporation is an S Corporation
- The reason why tax expense is not provided, including the fact that income is taxable to the stockholders of the corporation
- The net differences between the tax bases and the reported amounts of the corporation's assets and liabilities
- If relevant to the users of the financial statements, the components of retained earnings, including such items as preelection accumulations, shareholders' undistributed taxable income previously taxed, the accumulated adjustment account, and other adjustment accounts

Illustrative examples of disclosure of this information are presented in the remaining portion of this section.

Illustrative Disclosure of Tax Status

Note 1 — Nature of Business and Summary of Significant Accounting Policies

Income taxes: The Company, with the consent of its stockholders, has elected under the Internal Revenue Code to be taxed as an S Corporation. In lieu of corporate income taxes, the stockholders of an S Corporation are taxed on their proportionate share of the company's taxable income. Therefore, no provision or liability for federal income tax has been included in these financial statements.

Illustrative Disclosure of Tax Differences

Note 5 — Income Taxes

Income reported for tax purposes differs from net income because the Company reports contract revenues and expenses on a completed contract basis for taxation and because of differences in depreciation accounting. At December 31, 19X4, differences between earnings previously taxed and book retained earnings is primarily due to the following temporary differences:

Contracts in process, timing of recognition of gross profit	$342,000
Depreciation, accelerated methods for tax purposes	$ 14,100

Illustrative Disclosure of Components of Retained Earnings

Note 10 — Retained Earnings

Retained earnings consist of the following at December 31, 19X5:

Federal tax basis accumulated earnings account		$ 683,700
Accumulated Adjustment Account:		
Beginning balance, January 1, 19X5	$ 553,326	
Ordinary taxable income	375,658	
Separately computed income	93,266	
Separately computed deductions	(13,345)	
Nondeductible expenses	(5,938)	
Dividend distributions	(600,000)	
Ending balance, December 31, 19X5		402,967

Tax Timing Account:		
Beginning balance, January 1, 19X5	$ 331,485	
Gross profit on contracts in process	349,492	
Income from partnership investment	(89,580)	
Book/tax depreciation difference	(26,429)	
Franchise taxes	3,385	
Ending balance, December 31, 19X5		568,353
Retained earnings at December 31, 19X5		$1,655,020

Dividend distributions: During the year ended December 31, 19X5, the Company's Board of Directors declared dividends of $600,000, which were distributed to stockholders of outstanding shares of the Company's stock.

14.500 DEVELOPMENT STAGE ENTERPRISES

14.501 A development stage enterprise is one that devotes substantially all of its efforts to establishing a new business and in which either planned principal operations have not commenced, or planned principal operations have commenced, but there has been no significant revenue.

14.502 Generally accepted accounting principles that apply to other companies also apply to development stage enterprises. Accordingly, development stage enterprises should defer only those costs that established operating companies would be permitted to defer under GAAP.

Unique Disclosures of Development Stage Enterprises

14.503 Disclosures that are unique to development stage enterprises include:

- Identification of the financial statements as those of a development stage enterprise
- A description of the nature of the development stage activities
- Identification of cumulative net losses with a descriptive caption such as "Accumulated Deficit During the Development Stage"
- Presentation in the income statement of amounts of revenues and expenses for each period presented and cumulative amounts since inception of the enterprise
- Presentation in the statement of cash flows the cash flows for each period presented and cumulative amounts since inception of the enterprise
- Details about issuance of stock and other equity securities since inception of the enterprise

Illustrative Financial Statements

14.504 The pages that follow contain illustrative financial statements for a development stage enterprise.

14.505 Illustrative Financial Statements of a Development Stage Enterprise

Lyle Home Entertainment, Inc.
(A Development Stage Enterprise)
Balance Sheet
December 31, 19X7

ASSETS	
Current Assets	
Cash	$5,332
Inventory (Note 1)	10,603
Prepaid expenses	19,821
Total current assets	35,756
Furniture and equipment, net of accumulated depreciation of $404 (Note 1)	2,447
Other assets	
Organization costs, net (Note 1)	1,342
Deposits	1,050
	$40,595
LIABILITIES AND STOCKHOLDER'S EQUITY	
Current liabilities	
Accounts payable	$12,071
Customer deposit	10,000
Total current liabilities	22,071
Advances from parent (Note 2)	161,382
Commitments (Notes 4 and 5)	
Stockholder's Equity	
Common stock, 1,000,000 shares authorized, 25,000 shares issued and outstanding	25,000
Deficit accumulated during the development stage	(167,858)
	(142,858)
	$40,595

See accountant's review report and notes to financial statements.

Lyle Home Entertainment, Inc.
(A Development Stage Enterprise)
Statements of Operations
Year Ended December 31, 19X7 and the Period
from November 8, 19X6 (Inception) to December 31, 19X7

	Year Ended December 31, 19X7	Period from November 8, 19X6 (Inception) to December 31, 19X7
Sales	$ —	$ —
Cost of sales	—	—
Gross profit	—	—
Selling, general and administrative expenses	142,480	167,680
Operating loss	142,480	167,680
Interest income	(222)	(222)
Net loss before income taxes	142,258	167,458
State income taxes (Note 3)	400	400
Net loss	$ 142,658	$ 167,858

See accountant's review report and notes to financial statements.

Lyle Home Entertainment, Inc.
(A Development Stage Enterprise)
Statement of Stockholder's Equity
Period from November 8, 19X6 (Inception) to December 31, 19X7

Accumulated Stock	Common Deficit	
Issuance of 25,000 shares (November 8, 19X6)	$ 25,000	$ —
Net loss	—	167,858
Balance, December 31, 19X7	$ 25,000	$ 167,858

See accountant's review report and notes to financial statements.

Lyle Home Entertainment, Inc.
(A Development Stage Enterprise)
Statements of Cash Flows
Year Ended December 31, 19X7 and the Period
from November 8, 19X6 (Inception) to December 31, 19X7

	Year Ended December 31, 19X7	Period from November 8, 19X6 (Inception) to December 31, 19X7
Cash Flows from Operating Activities		
Net loss	$(142,658)	$(167,858)
Adjustments to reconcile net loss to cash flow used by operating activities:		
Depreciation and amortization	739	739
Increase in inventory	(10,603)	(10,603)
Increase in prepaid expenses	(14,521)	(19,821)
Increase in deposits	(1,050)	(1,050)
Increase in accounts payable	3,471	12,071
Increase in customer deposit	10,000	10,000
Net Cash Used by Operating Activities	(154,622)	(176,522)
Cash Flows from Investing Activities		
Purchase of furniture and equipment	(2,851)	(2,851)
Payment of organization costs	—	(1,677)
Net Cash Used by Investing Activities	(2,851)	(4,528)
Cash Flows from Financing Activities		
Issuance of common stock	—	25,000
Advances from parent	161,382	161,382
Net Cash from Financing Activities	161,382	186,382
Net Increase in Cash	3,909	5,332
Cash at Beginning of Period	1,423	—
Cash at End of Period	$ 5,332	$ 5,332

See accountant's review report and notes to financial statements.

Lyle Home Entertainment, Inc.
(A Development Stage Enterprise)
Notes to Financial Statements

Note 1 — Nature of Business and Significant Accounting Policies

The Company, incorporated in California on November 8, 19X6, is a wholly owned subsidiary of Ronson Inc., a Delaware corporation. The Company was formed to distribute and sell video cassette rental machines in Southwest U.S.A. and to operate machines owned by the Company.

As a development stage enterprise, most of management's efforts have been devoted to promoting the Company's product and organizing for its manufacture, storage, distribution and servicing.

Inventory: Inventory is recorded at lower of cost or market on a specific identification basis.

Furniture and Equipment: Furniture and equipment are recorded at cost. Depreciation is provided on the straight-line method over the estimated useful lives of the assets.

Organization Costs: Costs incurred to organize the Company have been capitalized and are being amortized over five years.

Income Taxes: Differences exist between the methods of accounting for financial statement and income tax purposes, primarily in the treatment of start-up costs and depreciation.

Use of estimates. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note 2 — Advances From Parent

Amounts advanced from the parent company are noninterest bearing and unsecured. These advances are classified as long-term obligations.

Note 3 — Income Taxes

Differences between the amount of losses reflected on the statements of operations and that reported for income tax purposes arise primarily from the capitalization of development stage expenses for income tax purposes. Current tax expense is as follows:

Federal	$ —
State	400
	$ 400

As of December 31, 19X7, a loss carryforward of $165,392 that expires in 19Y4 is available to offset future taxable income.

Lyle Home Entertainment, Inc.
(A Development Stage Enterprise)
Notes to Financial Statements(Continued)

Note 4 — Related-Party Transactions

The Company has entered into an agreement with Ultra Corporation to provide it with management services and personnel. Ultra Corporation is wholly owned by an officer of the Company.

Under the terms of the agreement, Ultra is to be paid the greater of ten percent of Company profits or $12,000 per year in addition to a basic management fee of $4,000 per month. Any other expenses incurred on behalf of the Company are reimbursed on a monthly basis.

Included in the accompanying statements of operations are $56,400 and $61,200 in management fees, and $8,062 and $10,222 in expense reimbursements paid to Ultra Corporation for the year ended December 31, 19X7 and the period from November 8, 19X6 (inception) to December 31, 19X7, respectively.

Note 5 — Leasing Arrangements

The Company leases office and warehouse space under two separate agreements on a month-to-month basis with combined monthly payments of $1,050. Total rent expense was $7,316 and $8,366, for the year ended December 31, 19X7 and the period from November 8, 19X6 (inception) to December 31, 19X7, respectively.

14.600

Disclosure Checklist for Nonpublic Entities

Client: ____________________

Financial Statement Date: ____________________

Preparer: ____________________ Date: ____________

INSTRUCTIONS:

This checklist is designed to evaluate financial statement disclosures in review and full disclosure compilation engagements. Part I is a checklist of disclosures that are applicable to most financial statements. Part II is a checklist of disclosures that are not commonly required; only the applicable section(s) of Part II should be completed for those engagements for which the disclosures apply. N/A should be checked for disclosures that do not apply to the entity, or for disclosures that are not necessary because the item or information is immaterial. When reviewing or compiling financial statements of clients in specialized industries, the accountant should refer to other accounting pronouncements and AICPA audit and accounting guides for additional required disclosures.

EXPLANATION OF REFERENCES:			
ARB	*Accounting Research Bulletin*	**APB**	*Accounting Principles Board Opinion*
SFAS	*Statement of Financial Accounting Standards*	**SAS**	*Statement on Auditing Standards*
FASBI	*Financial Accounting Standards Board Interpretation*	**TB**	*Technical Bulletin issued by the staff of the FASB*
SSARS	*Statements on Standards for Accounting and Review Services*	**PB**	*AICPA Accounting Standards Division Practice Bulletin*

PART I — COMMON DISCLOSURES

GENERAL	Yes	No	N/A
Titles, References, and Accounting Policies			
1. Are the financial statements appropriately titled? [SAS 62, par. 7]	___	___	___
2. Does each statement include a general reference to the financial statement notes?	___	___	___

	Yes	No	N/A
3. Are the notes referenced from the appropriate statement items and appropriately titled?	___	___	___
4. Is a description of all significant accounting policies of the reporting entity presented as an integral part of the financial statements? [APB 22, par. 8]	___	___	___
Comparative Financial Statements			
1. Are the financial statement disclosures related to the comparative financial statements adequate? [ARB 43, Ch. 2A, par. 2]	___	___	___
2. If changes have occurred in the manner of or basis for presenting corresponding items for two or more periods, are appropriate explanations of the changes disclosed? [ARB 43, Ch. 2A, par. 3]	___	___	___
Related-Party Transactions and Economic Dependency			
1. For related-party transactions, do disclosures include:			
a. The nature of the relationship(s) involved (e.g., affiliate companies, owners, officers, etc.)?	___	___	___
b. A description of the transactions, including those to which no amounts or nominal amounts were ascribed, for each of the periods for which income statements are presented, and such other information deemed necessary to an understanding of the effects of the transactions on the financial statements?	___	___	___
c. The dollar amounts of transactions for each of the periods for which income statements are presented and the effects of any change in the method of establishing the terms from that used in the preceding period?	___	___	___
d. Amounts due from or to related parties as of the date of each balance sheet presented and, if not otherwise apparent, the terms and manner of settlement? [SFAS 57, pars. 2–4]	___	___	___
2. Is information about economic dependency on one or more customers or suppliers disclosed when necessary for a fair presentation? [SFAS 21, par. 9]	___	___	___

	Yes	No	N/A
3. Is the nature of a controlled relationship disclosed, even though there are no transactions between the enterprises, if the reporting enterprise and one or more other enterprises are under common ownership or management control and the existence of the control could result in operating results or financial position of the reporting enterprise significantly different from those that would have been obtained if the enterprises were autonomous? [SFAS 57, pars. 2 and 4]	___	___	___

Contingencies, Commitments, and Questions About the Entity's Ability to Continue as a Going Concern

	Yes	No	N/A
1. Are the nature and amount of accrued loss contingencies disclosed as necessary to keep the financial statements from being misleading? [SFAS 5, par. 9]	___	___	___
2. For loss contingencies not accrued, do disclosures indicate:			
a. The nature of the contingency?	___	___	___
b. An estimate of possible loss or range of loss, or a statement that such estimate cannot be made? [SFAS 5, par. 10]	___	___	___
3. If exposure to loss exists in excess of the amount accrued for a loss contingency do disclosures include an estimate of the excess amount or a statement that no estimate is possible? [SFAS 5, par. 10]	___	___	___
4. Are the nature and amount of guarantees disclosed (for example, guarantees of indebtedness of others, obligations of banks under standby letters of credit, or guarantees to repurchase receivables that have been sold or otherwise assigned)? [SFAS 5, par. 12; FASBI 34, pars. 1–3]	___	___	___
5. If conditions and events exist that indicate the entity may be unable to continue as a going concern, has consideration been given to the need to disclose:			
a. The principal conditions and events that indicate the going concern problem?	___	___	___
b. Management's évaluation of the significance of these conditions an events?	___	___	___

	Yes	No	N/A
c. The possible effects of such conditions and events, including the possible effects on the recoverability or classification of assets and the amounts or classification of liabilities?	___	___	___
d. Mitigating factors, including management's plans? [SAS 59, par. 11; Interpretation No. 11 of SSARS 1]	___	___	___
6. Do the financial statements include the following disclosures about risks and uncertainties?			
a. Nature of operations.	___	___	___
b. Use of estimates in the preparation of financial statements.	___	___	___
c. Certain significant estimates (if certain conditions are met).	___	___	___
d. Current vulnerability due to certain concentrations (if certain conditions are met).	___	___	___
7. Is there adequate disclosure of commitments, such as commitments to purchase capital expenditures, inventory purchase agreements, and employment contracts? [SFAS 5, pars. 18–19; ARB 43, Ch. 4, par. 17]	___	___	___

Subsequent Events

	Yes	No	N/A
1. Are the financial statements adjusted for any changes in estimates resulting from subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet? [SFAS 5, par. 8; SAS 1, secs. 560.03–.04 and .07, and 561.01–.09]	___	___	___
2. Are subsequent events that provide evidence with respect to conditions that did not exist at the date of the balance sheet but arose subsequent to that date adequately disclosed to keep the financial statements from being misleading? [SFAS 5, par. 11; APB 16, par. 61; SAS 1, secs. 560.05–.07 and .09, and 561.01–.09]	___	___	___

	Yes	No	N/A
Pension Plans — Defined Contribution			
1. Is the following information disclosed about the entity's defined contribution plan:			
a. A description of the plan(s) including employee groups covered, the basis for determining contributions, and the nature and effect of significant matters affecting comparability of information for all periods presented?	___	___	___
b. The amount of cost recognized during the period? [SFAS 87, par. 65]	___	___	___
Advertising Costs			
1. Do disclosures for advertising costs include:			
a. The accounting policy selected from the two alternatives in the beginning of paragraph 26 of SOP 93-7 (as interpreted by PB 13, *Direct Response Advertising and Probable Future Benefits*) for reporting advertising, indicating whether such costs are expensed as incurred or the first time the advertising takes place?	___	___	___
b. A description of the direct-response advertising reported as assets (if any), the accounting policy for it, and the amortization period?	___	___	___
c. The total amount charged to advertising expense for each income statement presented, with separate disclosure of amounts, if any, representing a write-down to net realizable value?	___	___	___
d. The total amount of advertising reported as assets in each balance sheet presented? [SOP 93-7, par 49]	___	___	___
Limited Liability Companies (LLCs) [PB 14]			
1. Are the financial statements clearly identified as being those of an LLC?	___	___	___
2. If the LLC has a finite life, do disclosures include the date the LLC will cease to exist?	___	___	___
3. Do disclosures include:			
a. A description of any limitation of an LLC member's liability?	___	___	___

	Yes	No	N/A
b. The different classes of member's interest and the respective rights, preferences, and privileges of each class?	___	___	___
4. Are all disclosures regarding members' equity and changes in members' equity for the period made?	___	___	___
5. Are all disclosures relating to the conversion of the entity to an LLC made?	___	___	___

BALANCE SHEET

1. For classified balance sheets, are assets and liabilities segregated into current and noncurrent classifications with totals presented for both current assets and current liabilities? [ARB 43, Ch. 3A; SFAS 6, par. 15; FASBI 8, par. 3; TB 79-3]	___	___	___
2. Are valuation allowances for assets such as receivables and investments shown as deductions from their related assets with appropriate disclosure? [APB 12, par. 3]	___	___	___

Cash

1. Are restrictions on cash appropriately disclosed? [SFAS 5, pars. 18-19]	___	___	___
2. Is cash that is restricted as to withdrawal or designated for use to acquire noncurrent assets or pay noncurrent debt appropriately segregated from cash available for current operations? [ARB 43, Ch. 3A, par. 6]	___	___	___
3. Are material bank overdrafts presented as liabilities?	___	___	___

Receivables

1. Are other significant types of receivables segregated from normal trade receivables?	___	___	___
2. Are allowances for uncollectible receivables disclosed? [APB 12, par. 3]	___	___	___
3. If a note is noninterest bearing or was issued at an unreasonable stated interest rate:			
a. Is the discount or premium presented as a deduction from or addition to the face amount of the note?	___	___	___

	Yes	No	N/A
b. Does the disclosure include the effective interest rate and face amount of the note?	___	___	___
c. Is amortization of discount or premium included in interest income in the income statement? [APB 21, par. 16]	___	___	___
4. For transfers of receivables with recourse that are reported as sales, are the following disclosed:			
a. The proceeds to the entity for each period for which an income statement is presented?	___	___	___
b. The information required by SFAS 105, including the face amount of the receivables; the nature and terms of the receivables; information about the entity's collateral policy, a description of the collateral and the entity's access to it; and the potential loss if the debtors failed to perform according to the terms of the receivables and the collateral proved to be of no value? [SFAS 77, par. 9; SFAS 105, pars. 17–18 as amended by SFAS 119, par. 14]	___	___	___
5. If the entity has significant concentrations of credit risk arising from accounts receivable, are the following disclosures provided about each significant concentration (unless the information about the concentration is apparent from the description of the business)?			
a. Information about the activity, region, or economic characteristics that identifies the concentration.	___	___	___
b. The dollar amount of the potential loss if the receivables prove to be of no value.	___	___	___
c. Information about the entity's collateral policies, access to collateral, and a description of the collateral. [SFAS 105, par. 20]	___	___	___
6. Are all fair value disclosures made with regard to accounts receivable? [SFAS 107, pars. 10, as amended by SFAS 119, pars. 14 and 15)	___	___	___

Inventories

	Yes	No	N/A
1. Are the major classes of inventory disclosed (e.g., finished goods, work in process, raw materials)? [ARB 43, Ch. 3A, pars. 4 and 9; ARB 43, Ch. 4, par. 3]	___	___	___
2. Is the method of determining inventory cost (e.g., LIFO, FIFO disclosed? [ARB 43, Ch. 3A, par. 9; ARB 43, Ch. 4, pars. 4–16; APB 22, par. 14]	___	___	___
Property and Equipment			
1. For depreciable assets, do the financial statements or notes thereto include disclosure of:			
a. Depreciation expense for each period? [APB 12, par. 5a]	___	___	___
b. Balances of major classes of depreciable assets by nature or function? [APB 12, par. 5b]	___	___	___
c. Accumulated depreciation, either by major classes of assets or in total? [APB 12, par. 5c]	___	___	___
d. The method or methods used in computing depreciation for major classes of depreciable assets? [APB 12, par. 5d; APB 22, par. 14]	___	___	___
2. Are assets that are not used for operations (e.g., idle or held for investment) segregated from other plant and equipment?	___	___	___
3. If SFAS 121 has been adopted, have the following disclosures been included in the financial statements:	___	___	___
a. Disclosures required if an impairment loss is recognized for assets to be held or used, such as a description of the assets and impairment, amount of impairment, how the fair value was determined, and the income statement caption in which the impairment loss is aggregated. [Refer to SFAS 121, par. 14]	___	___	___
b. Disclosures required for assets disposed of in accordance with paragraphs 15-17 of SFAS 121, such as a description and carrying amount of the assets, the loss resulting from application of paragraph 15, the gain or loss resulting from the application of paragraph 17, the income statement caption in which the gains or losses are aggregated, and the result of operations for the assets. [Refer to SFAS 121, par. 19]	___	___	___

	Yes	No	N/A

Current Liabilities

	Yes	No	N/A
1. Do current liabilities include the following amounts (appropriately segregated by category)?	___	___	___
a. Accrued liabilities.	___	___	___
b. Collections received in advance of the delivery of goods or performance of services.	___	___	___
c. Other liabilities whose regular and ordinary liquidation is expected to occur within a relatively short time period.	___	___	___
d. Obligations that, by their terms, are due on demand or will be due within one year (or operating cycle, if longer) from the balance-sheet date.	___	___	___
e. Long-term obligations that because of violations of debt provisions (without appropriate waivers from creditors) cause the obligation to be currently payable on demand, or potentially payable on demand within one year from the balance-sheet date. [ARB 43, Ch. 1, par. 5; ARB 43, Ch. 3A, pars. 7–8; SFAS 78, par. 5]	___	___	___

Notes Payable and Other Debt

	Yes	No	N/A
1. Is there adequate disclosure of interest rates, maturities, and other terms and conditions of loan agreements, such as assets pledged as collateral, covenants to restrict debt, maintain working capital, and restrict dividends? [SFAS 5, pars. 18–19]	___	___	___
2. Are the combined aggregate amounts of maturities for all long-term borrowings for each of the five years following the date of the latest balance sheet disclosed? [SFAS 47, par. 10b]	___	___	___
3. If the note is noninterest bearing or was issued with an unreasonable stated interest rate:			
a. Is the discount or premium presented as a deduction from or addition to the face amount of the note?	___	___	___
b. Does the disclosure include the effective interest rate and face amount of the note?	___	___	___

	Yes	No	N/A
c. Is amortization of the discount or premium included in interest expense in the income statement? [APB 21, par. 16]	___	___	___
4. Are current portions of debt obligations presented as current liabilities? [ARB 43, Ch. 3A, pars. 7–8]	___	___	___
5. If an obligation is excluded from current liabilities because it is expected to be refinanced on a long-term basis, do disclosures include:			
a. A general description of the financing agreement?	___	___	___
b. Terms of any new obligation incurred or expected to be incurred, or equity securities issued or expected to be issued as a result of the refinancing? [SFAS 6, par. 15; FASBI 8, par. 3; TB 79-3]	___	___	___

Lease Obligations

	Yes	No	N/A
1. For capital leases, do disclosures include:			
a. Gross amounts of assets recorded by major classes as of the date of each balance sheet presented? (These may be combined with owned assets.) [SFAS 13, par. 16a]	___	___	___
b. Presentation of lease obligations appropriately segregated by current and long-term portions?	___	___	___
c. Future minimum lease payments as of the latest balance sheet presented in the aggregate and for each of the five succeeding fiscal years with appropriate separate deductions for executory costs and imputed interest to reduce net minimum lease payments to present value? [SFAS 13, pars. 10 and 16a]	___	___	___
d. Total of future minimum sublease rentals under noncancelable subleases as of the date of the latest balance sheet presented? [SFAS 13, par. 16a]	___	___	___
e. Total contingent rentals actually incurred for each period for which an income statement is presented? [SFAS 13, par. 16a; SFAS 29, par. 12]	___	___	___

	Yes	No	N/A
f. Assets recorded under capital leases and the related accumulated amortization and obligations under the lease identified separately in the balance sheet or a note? [SFAS 13, par. 13]	___	___	___
2. For operating leases that have initial or remaining noncancelable lease terms in excess of one year, do disclosures include:			
a. Future minimum rental payments required as of the latest balance sheet presented in the aggregate and for each of the five succeeding fiscal years?	___	___	___
b. The total of future minimum rentals under noncancelable subleases as of the date of the latest balance sheet presented? [SFAS 13, par. 16b]	___	___	___
3. For all operating leases, do disclosures include rental expense for each period for which an income statement is presented with separate amounts for minimum rentals, contingent rentals, and sublease rentals? [SFAS 13, par. 16c]	___	___	___
4. Do disclosures include a general description of the lessee's leasing arrangements including but not limited to:			
a. Bases for determination of contingent rentals?	___	___	___
b. Terms of any renewal or purchase options or escalation clauses?	___	___	___
c. Restrictive covenants? [SFAS 13, par. 16d]	___	___	___

Income Taxes

	Yes	No	N/A
1. Have the types of significant temporary differences and carryforwards been disclosed? [SFAS 109, par. 44]	___	___	___
2. Have the significant components of income tax expense attributable to continuing operations for each year presented been disclosed in the financial statements or notes? [SFAS 109, par. 45]	___	___	___

	Yes	No	N/A
3. Has the amount of income tax expense or benefit allocated to continuing operations and the amounts separately allocated to other items (in accordance with the provisions of paragraphs 35-39 of SFAS 109) been disclosed for each year for which those items are presented? [SFAS 109, par. 46]	___	___	___
4. Has the nature of the significant reconciling items (in SFAS 109, par. 47) been disclosed?	___	___	___
5. Have the amounts and expiration dates of operating loss and tax credit carryforwards for tax purposes been disclosed? [SFAS 109, par. 48]	___	___	___
6. Has the effect of initially applying SFAS 109 been reported as the effect of a change in accounting principle in a manner similar to the cumulative effect of a change in accounting principle (APB 10, paragraph 20) except for initially recognized tax benefits of the type required by SFAS 109 to be excluded from comprehensive income? [SFAS 109, par. 51]	___	___	___
7. When initially presented, have the financial statements for the year SFAS 109 is first adopted disclosed the following:			
a. The effect, if any, of adopting SFAS 109 on pretax income from continuing operations (for example, the effect of adjustments for prior purchase business combinations and for regulated enterprises) for the year of adoption if restated financial statements for the prior year are not presented?	___	___	___
b. The effect of any restatement on income from continuing operations, income before extraordinary items, and net income (and on related per share amounts) for each year for which restated financial statements are presented? [SFAS 109, par. 52]	___	___	___
Other Liabilities			
1. Are estimated losses from loss contingencies accrued if both "probable" as explained in SFAS 5 and the amount can be reasonably estimated? [SFAS 5, par. 8; FASBI 14]	___	___	___
2. Are liabilities appropriately accrued and reported for employees' compensation for future absences? [SFAS 43, pars. 6–7]	___	___	___

	Yes	No	N/A
Stockholders' Equity			
1. For each class of stock, do disclosures include the number of shares authorized, issued and outstanding, and par or stated value per share?	___	___	___
2. Do the financial statements include a description, in summary form, sufficient to explain the pertinent rights and privileges of the various securities outstanding; for example: dividend and liquidation preferences participation rights, buy-sell agreements, and unusual voting rights? [APB 15, par. 19]	___	___	___
3. Are stock option and compensation agreements accounted for properly and adequately disclosed? [APB 25, par. 8]	___	___	___
4. Are changes in the separate component accounts of stockholders' (owners') equity disclosed? [APB 12, par. 10]	___	___	___
5. Are changes in the number of shares of equity securities disclosed? [APB 12, par. 10]	___	___	___
INCOME STATEMENT			
1. Are the important components of income, such as sales, other sources of revenue, cost of sales, selling and administrative expenses, interest expense and income taxes separately disclosed?	___	___	___
2. Is the amount of interest cost incurred disclosed in the statements or notes thereto, and for an accounting period in which some interest cost is capitalized, is the total amount thereof that has been capitalized disclosed? [SFAS 34, par. 21]	___	___	___
3. Are extraordinary items segregated and shown (including applicable income taxes) following income before extraordinary items and before net income? [APB 30, pars. 10–12]	___	___	___
4. Do disclosures include descriptions of any extraordinary event(s) or transaction(s) and the principal items entering into determination of extraordinary gain(s) or loss(es)? [APB 30, par. 11]	___	___	___
5. Are material events or transactions that are either unusual in nature or of infrequent occurrence but not both:			

	Yes	No	N/A
a. Reported as a separate component of income from continuing operations?	___	___	___
b. Accompanied by disclosure of the nature and financial effects of each event? [APB 30, par. 26; TB 82-1, par. 6]	___	___	___

STATEMENT OF CASH FLOWS

	Yes	No	N/A
1. Is a statement of cash flows presented as a basic financial statement for each period for which a statement of income is presented? [SFAS 95, par. 3]	___	___	___
2. Does the statement of cash flows explain the change in cash or cash and cash equivalents for the period? [SFAS 95, par. 7]	___	___	___
3. Is the policy for defining a cash equivalent disclosed? [SFAS 95, par. 10]	___	___	___
4. Does the statement segregate net cash flows from operating, investing and financing activities? [SFAS 95, par. 6]	___	___	___
5. Are cash receipts and cash payments for the following transactions classified as cash flows from investing activities:			
a. Receipts from collections or sales of loans or investments in debt instruments?	___	___	___
b. Receipts from the sales of investments in stock?	___	___	___
c. Receipts from sales of property, plant and equipment and other productive assets?	___	___	___
d. Payments for loans to others and investments in debt instruments?	___	___	___
e. Payments to acquire property, plant and equipment and other productive assets?	___	___	___
f. Payments to acquire investments in stock? [SFAS 95, pars. 16–17]	___	___	___
6. Are cash receipts and cash payments for the following transactions classified as cash flows from financing activities:			

	Yes	No	N/A
a. Proceeds from issuing debt or the entity's stock?	___	___	___
b. Repayments of amounts borrowed?	___	___	___
c. Payments to reacquire the entity's stock? [SFAS 95, pars. 19-20]	___	___	___
7. Does the statement or a separate schedule provide a reconciliation of net income to net cash flow from operating activities? [SFAS 95, pars. 28-30]	___	___	___
8. Are noncash investing and financing activities (i.e., converting debt to equity) summarized in a separate schedule? [SFAS 95, par. 32]	___	___	___

PART II — OTHER DISCLOSURES

INSTRUCTIONS

For topics included in this portion of the disclosure checklist that are *not applicable* (because the entity does not have transactions or accounts related to these topics or the transactions or accounts are immaterial), check "N/A" by the section heading and go to the next section.

Yes No N/A

Accounting Changes and Corrections of Errors

1. For an accounting change (including one that is expected to have a material effect in the future) does disclosure in the period of the change include:

   a. The nature of the change? ___ ___ ___

   b. Justification for the change? ___ ___ ___

   c. Effect on income? ___ ___ ___

   [APB 20, par. 17]

2. For a change in accounting principle that is accounted for by presenting the cumulative effect of the change separately in the income statement between the captions "extraordinary items" and "net income," does disclosure include either:

   a. The pro forma amounts of income before extraordinary items and net income for each period presented (shown on the face of the financial statements), as if the principle was adopted for that period (If only one period is presented, amounts for the immediate prior period should be presented.) or ___ ___ ___

   b. Disclosure of the fact that the amounts are not presented because the pro forma amounts cannot be determined? ___ ___ ___

   [APB 20, pars. 18–26]

3. If the cumulative effect of the change cannot be determined (e.g., a change from FIFO to LIFO) is disclosure included of the effect of the change on the results of operations for the period of the change, and the reasons for not presenting the cumulative effect? ___ ___ ___
   [APB 20, par. 26]

4. For a change in accounting principle that is accounted for by restating prior periods (e.g., a change from LIFO method of inventory pricing to another method) is the change shown by adjusting retained earnings and restating comparative financial statements (if possible)? ___ ___ ___
   [APB 20, pars. 27–28]

5. Is the correction of an error shown as a prior-period adjustment with disclosure of the following in the period of its discovery and correction:

   a. Nature of the error in previously issued financial statements? ___ ___ ___

	Yes	No	N/A

Accounting Changes and Corrections of Errors (Continued)

b. Effect of its correction on income before extraordinary items and net income? [APB 20, pars. 36–37; SFAS 16, par. 11] ___ ___ ___

Business Combinations

1. If a business combination occurred during the period that met the specific conditions for a pooling of interests [APB 16, pars. 45–48]:

   a. Has the required accounting method been applied? [APB 16, pars. 50–62] ___ ___ ___

   b. Do the statements and notes include the appropriate disclosures? [APB 16, pars. 63–65] ___ ___ ___

2. If a business combination does not meet the specified conditions for a pooling of interests:

   a. Has the combination been accounted for by the purchase method? [APB 16, pars. 66–94; SFAS 38; TB 81-2, par. 4] ___ ___ ___

   b. Do the statements and notes include the required disclosures? [APB 16, pars. 95–96; SFAS 79, pars. 4–6] ___ ___ ___

Consolidations

1. If consolidated statements are presented:

   a. Is the consolidation policy disclosed? [ARB 51, par. 5; APB 22, par. 14] ___ ___ ___

   b. Are intercompany balances and transactions eliminated? [ARB 51, par. 6] ___ ___ ___

   c. In instances when the financial reporting periods of subsidiaries differ from those of the parent, is recognition given to the effect of intervening events that materially affect financial position or the results of operations? [ARB 51, par. 4; SFAS 12, pars. 18–20; FASBI 14] ___ ___ ___

	Yes	No	N/A

Discontinued Operations

1. Is operation of a segment that has been discontinued or is the subject of a formal plan for disposition:

   a. Reported separately from income from continuing operations (including applicable taxes) and as a component of income before extraordinary items? ___ ___ ___
   [APB 30, pars. 8 and 14–18]

   b. Accompanied by disclosure in the notes of revenue applicable to the discontinued operations? ___ ___ ___
   [APB 30, par. 8]

2. Is gain or loss (or estimated loss) from disposal of a discontinued segment reported separately (including applicable income taxes) in conjunction with results of discontinued operations? ___ ___ ___
   [APB 30, pars. 14–18]

3. For the period encompassing the measurement date, do the financial statements disclose:

   a. Identity of the segment discontinued? ___ ___ ___

   b. Expected disposal date, if known? ___ ___ ___

   c. Expected manner of disposal? ___ ___ ___

   d. Description of the remaining assets and liabilities of the discontinued segment at the balance-sheet date? ___ ___ ___

   e. Income or loss from operations and any proceeds from disposal of the discontinued segment during the period from the measurement date to the balance-sheet date? ___ ___ ___

   [APB 30, par. 18]

4. For periods after the measurement date, do notes to financial statements disclose the information required for the period encompassing the measurement date and the actual date and results of disposal compared with the prior estimates? ___ ___ ___
   [APB 30, par. 18]

	Yes	No	N/A
Extinguishment of Debt			
1. If there is an extinguishment of debt, is the difference between reacquisition price and carrying amount:			
a. Recognized currently in income?	___	___	___
b. Treated as an extraordinary gain or loss?	___	___	___
Financial Instruments Including Derivatives (SFAS 119 is effective for financial statements issued for fiscal years ending after December 15, 1994, except for entities with less than $150 million in total assets, for which it is effective for fiscal years ending after December 15, 1995. In addition to requiring disclosures related to derivatives, SFAS 119 expands and amends SFASs 105 and 107.) [SFASs 105, 107, and 119]			
1. Are all disclosures (including contract amount, nature and terms, amount of accounting loss at risk, and the entity's policies) for all financial instruments (those with and without off-balance-sheet risk) included in the body of the financial instrument? [Refer to SFAS 105, pars. 17 and 18, as amended by SFAS 119, par. 14, and SFAS 119, pars. 8 and 9 for required disclosures.]	___	___	___
2. Are all significant concentrations of credit risk arising from all financial instruments disclosed?	___	___	___
3. Are all fair value disclosures made with regard to all financial instruments?	___	___	___
4. Do the disclosures in Steps 1 and 3 distinguish between financial instruments held for trading purposes and those held for purposes other than trading?	___	___	___
5. If the offsetting of derivatives against nonderivatives is not permitted under FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts*, does the entity, when disclosing the fair value of derivatives, not combine, aggregate, or net the fair values?	___	___	___
6. Are all disclosures for derivatives held for purposes other than trading included in the financial statements? (Note: small businesses rarely hold derivatives for trading purposes; therefore, disclosures for such derivatives are not included in this checklist. If the entity holds derivatives for trading purposes, refer to SFAS 119 for required disclosures.)	___	___	___

	Yes	No	N/A
Investments			
1. Is the equity method used to account for investments in common stock of:			
a. Corporate joint ventures? [APB 18, par. 16]	___	___	___
b. Investees in which the entity has "ability to exercise significant influence" (generally presumed to be 20% or more of the voting stock)? [APB 18, par. 17; FASBI 35, pars. 2–5]	___	___	___
2. Are the disclosures listed in paragraph 20 of APB 18 made for investments in common stock accounted for by the equity method?	___	___	___
Debt and Equity Securities			
1. For securities classified as available-for-sale or held-to-maturity, are the following disclosed (by major security type)?			
a. Aggregate fair value,	___	___	___
b. Gross unrealized holding gains, and	___	___	___
c. Amortized cost basis. [SFAS 115, par. 19]	___	___	___
2. For investments in debt securities classified as available-for-sale or held-to-maturity, is disclosure made about their contractual maturities as of the latest balance sheet presented? [SFAS 115, par. 20]	___	___	___
3. For each period for which an income statement is presented, are the following disclosures made?			
a. The proceeds from sales of available-for-sale securities and the gross realized gains and losses from those sales,	___	___	___
b. The basis on which cost was determined in computing realized gain or loss, that is, specific identification, average cost, or other method used,	___	___	___
c. The gross gains and losses included in earnings from transfers of securities from the available-for-sale category to the trading category,	___	___	___

	Yes	No	N/A

Debt and Equity Securities (Continued)

d. The change in net unrealized holding gain or loss on available-for-sale securities that has been included in the separate component of shareholders' equity during the period, ___ ___ ___

e. The change in net unrealized holding gain or loss on trading securities that has been included in earnings during the period, and ___ ___ ___

f. For any sales of or transfers from held-to-maturity securities, 1) the amortized cost amount of the sold or transferred security, 2) the related realized or unrealized gain or loss, and 3) the circumstances leading to the decision to sell or transfer the security. ___ ___ ___

[SFAS 115, pars. 21 and 22]

Nonmonetary Transactions

1. Are nonmonetary transactions accounted for in conformity with APB 29? [APB 29, pars. 18–27] ___ ___ ___

2. Do disclosures for nonmonetary transactions during the period include:

   a. Nature of the transactions? ___ ___ ___

   b. Basis of accounting for the assets transferred? ___ ___ ___

   c. Gains or losses recognized on the transfers? ___ ___ ___

   [APB 29, par. 28; FASBI 30]

Pension Plans — Defined Benefit

1. Do disclosures include:

   a. A description of the plan including employee groups covered, type of benefit formula, funding policy, types of assets held and significant nonbenefit liabilities, if any, and the nature and effect of significant matters affecting comparability of information for all periods presented? ___ ___ ___

   b. The amount of net periodic pension cost for the period showing separately the service cost component, the interest cost component, the actual return on assets for the period, and the net total of other components? ___ ___ ___

   c. A schedule reconciling the funded status of the plan with amounts reported in the employer's statement of financial position, showing separately:

	Yes	No	N/A

Pension Plans — Defined Benefit (Continued)

	Yes	No	N/A
(1) The fair value of plan assets?	___	___	___
(2) The projected benefit obligation identifying the accumulated benefit obligation and the vested benefit obligation?	___	___	___
(3) The amount of unrecognized prior service cost?	___	___	___
(4) The amount of unrecognized net gain or loss (including asset gains and losses not yet reflected in market-related value)?	___	___	___
(5) The amount of any remaining unrecognized net obligation or net asset existing at the date of initial application of SFAS 87?	___	___	___
(6) The amount of any additional liability recognized pursuant to SFAS 87, paragraph 36?	___	___	___
(7) The amount of net pension asset or liability recognized in the statement of financial position pursuant to SFAS 87, paragraphs 35–36 (which is the net result of combining the preceding six items)?	___	___	___
d. The weighted-average assumed discount rate and rate of compensation increase (if applicable) used to measure the projected benefit obligation and the weighted-average expected long-term rate of return on plan assets?	___	___	___
e. If applicable, the amount and types of securities of the employer and related parties included in plan assets, and the approximate amount of annual benefits of employees and retirees covered by annuity contracts issued by the employer and related parties. Also, if applicable, the alternative amortization methods used pursuant to SFAS 87, paragraphs 26 and 33, and the existence and nature of the commitment discussed in paragraph 41?	___	___	___

[SFAS 87, par. 54]

Postretirement Benefits Other Than Pensions [SFAS 106]

1. If there are one or more defined benefit postretirement plans, do disclosures include—

	Yes	No	N/A
a. A description of the substantive plan(s) that is (are) the basis for the accounting?	___	___	___

	Yes	No	N/A

Postretirement Benefits Other Than Pensions [SFAS 106] (Continued)

	Yes	No	N/A
b. The amount of net periodic postretirement benefit cost?	___	___	___
c. A schedule reconciling the funded status of the plan(s) with amounts reported in the employer's statement of financial position?	___	___	___
d. The assumption and rates used in computing the expected postretirement benefit obligation and the accumulated postretirement benefit obligation (APBO) including the assumed health care cost trend rates; assumed discount rates; and the effect of a one-percentage-point increase in the assumed health care cost trend rate on the measurement of the APBO, the service cost, and the interest cost?	___	___	___
e. The amounts and types of securities of the employer and related parties included in plan assets and the approximate amount of future annual benefits of plan participants covered by insurance contracts issued by the employer and related parties?	___	___	___
f. Any alternative amortization method used pursuant to paragraphs 53 or 60 of SFAS 106?	___	___	___
g. The amount of gain or loss recognized during the period for a settlement or curtailment and a description of the nature of the event(s)?	___	___	___
h. The cost of providing special or contractual termination benefits recognized during the period and a description of the nature of the event(s)?	___	___	___
2. If there are one or more defined-contribution postretirement plans, have the following items been disclosed separately from defined benefit postretirement plan disclosures:			
a. A description of the plan(s)?	___	___	___
b. The amount of cost recognized during the period?	___	___	___

Stock Ownership Plans

1. If an employer sponsors an employee stock ownership plan (ESOP), do the employer's disclosures include:

Yes No N/A

Stock Ownership Plans (Continued)

a. A description of the plan, the basis for determining contributions, including the employee groups covered, and the nature and effect of significant matters affecting comparability of information for all periods presented?

   (1) For leveraged ESOPs and pension reversion ESOPs, the description should include the basis for releasing shares and how dividends on allocated and unallocated shares are used. ___ ___ ___

b. A description of the accounting policies followed for ESOP transactions, including the method of measuring compensation, the classification of dividends on ESOP shares, and the treatment of ESOP shares for EPS computations?

   (1) If the entity has both old ESOP shares for which it does not adopt the guidance in SOP 93-6 and new ESOP shares for which the guidance in SOP 93-6 is required, are the accounting policies for both blocks of shares disclosed? ___ ___ ___

c. The amount of compensation cost recognized during the period? ___ ___ ___

d. The number of allocated shares, committed-to-be-released shares, and suspense shares held by the ESOP at the balance-sheet date?

   (1) If the entity has both old ESOP shares for which it does not adopt the guidance in SOP 93-6 and new ESOP shares for which the guidance in SOP 93-6 is required, is the above disclosure made separately for both blocks of shares? ___ ___ ___

e. The fair value of unearned ESOP shares at the balance-sheet date for shares accounted for under SOP 93-6?[1] ___ ___ ___

f. The existence and nature of any repurchase obligation, including disclosure of the fair value of the shares allocated as of the balance-sheet date, which are subject to a repurchase obligation?[2] ___ ___ ___

---

[1] This disclosure need not be made for old ESOP shares for which the entity does not apply the guidance in SOP 93-6.

[2] Employers may wish to disclose additional information about the obligation, particularly information about the timing of payments. [SOP 93-6, par. 95]

	Yes	No	N/A
2. Are all the items listed in step 1 above disclosed even if the employer with an ESOP does not adopt SOP 93-6 for shares held by the ESOP on December 31, 1992? [SOP 93-6, par. 55]	___	___	___
3. For leveraged ESOPs and for nonleveraged ESOPs where the assets from the pension plan are used by the ESOP to purchase shares, when the employer reports the issuance of shares or the sale of treasury shares to the ESOP is the charge to unearned ESOP shares presented as a separate item in the balance sheet as a contra-asset account? [SOP 93-6, par. 13 and 46]	___	___	___
4. If the employer sponsors an ESOP with an indirect loan, is the outside loan reported as a liability and the receivable from the ESOP **not** reported on the employer's balance sheet? [SOP 93-6, par. 26]	___	___	___
5. If the employer sponsors an ESOP with an employer loan, is the ESOP's note payable and the employer's note receivable from the ESOP **not** reported in the employer's balance sheet? [SOP 93-6, par.27]	___	___	___
Troubled Debt Restructuring — Debtors			
1. For troubled debt restructuring occurring during the current period do disclosures include:			
a. A description of the principal changes in terms, the major features of settlement, or both?	___	___	___
b. The aggregate gain on restructuring of payables and the related income tax effect?	___	___	___
c. The aggregate net gain or loss on transfers of assets recognized during the period? [SFAS 15, par. 25]	___	___	___
2. For periods after a troubled debt restructuring, do disclosures include:			
a. The extent to which amounts contingently payable are included in the carrying amount of restructured payables?	___	___	___
b. Total amounts contingently payable, if applicable, and conditions under which those amounts would become payable or forgiven? [SFAS 15, par. 26]	___	___	___

14.700

Disclosure Checklist for Financial Statements Prepared on an Other Comprehensive Basis of Accounting (Tax or Cash Basis)

Client: ______________________________

Financial Statement Date: ______________________________

Preparer: ______________________________ Date: ______________

INSTRUCTIONS:

This checklist is designed to evaluate financial statement disclosures for financial statements prepared on an other comprehensive basis of accounting (tax or cash basis). Part I is a checklist of disclosures that are applicable to most financial statements. Part II is a checklist of disclosures that are not commonly applicable, only the applicable section(s) of Part II should be completed. N/A should be checked for disclosures that do not apply to the entity, or for disclosures that are not necessary because the item or information is immaterial. When reviewing or compiling financial statements of clients in specialized industries, the accountant should refer to other accounting pronouncements and AICPA audit and accounting guides for additional required disclosures. OCBOA financial statements and the related notes should be informative of matters that affect their use. In order to determine whether financial statement disclosures are adequate, you must have an understanding of the users and their needs. **The disclosures in this checklist should be considered for inclusion in OCBOA statements. The authors encourage you to carefully read paragraphs 9 and 10 of SAS 69 (AU 623).**

EXPLANATION OF REFERENCES:			
ARB	*Accounting Research Bulletin*	**APB**	*Accounting Principles Board Opinion*
SFAS	*Statement of Financial Accounting Standards*	**SAS**	*Statement on Auditing Standards*
FASBI	*Financial Accounting Standards Board Interpretation*	**TB**	*Technical Bulletin issued by the staff of the FASB*
SSARS	*Statements on Standards for Accounting and Review Services*	**PB**	*AICPA Accounting Standards Division Practice Bulletin*

PART I — COMMON DISCLOSURES

GENERAL

	Yes	No	N/A

Titles, References, and Accounting Policies

1. Are the financial statements appropriately titled? [SAS 62, par. 7] ___ ___ ___
2. Does each statement include a general reference to the financial statement notes? ___ ___ ___
3. Are the notes referenced from the appropriate statement items and appropriately titled? ___ ___ ___
4. Is a description of all significant accounting policies provided that describes the basis of presentation and how it differs from GAAP? ___ ___ ___
[SAS 62, par. 10]
5. Do the notes disclose the tax filing status of the entity (if other than a normal corporation)? ___ ___ ___

Comparative Financial Statements

1. Are the financial statement disclosures related to the comparative financial statements adequate? ___ ___ ___
[ARB 43, Ch. 2A, par. 2]
2. If changes have occurred in the manner of or basis for presenting corresponding items for two or more periods, are appropriate explanations of the changes disclosed? ___ ___ ___
[ARB 43, Ch. 2A, par. 3]

Related-Party Transactions and Economic Dependency

1. For related-party transactions, do disclosures include:
   a. The nature of the relationship(s) involved (e.g., affiliate companies, owners, officers, etc.)? ___ ___ ___
   b. A description of the transactions, including those to which no amounts or nominal amounts were ascribed, for each of the periods for which income statements are presented, and such other information deemed necessary to an understanding of the effects of the transactions on the financial statements? ___ ___ ___

GENERAL (Continued) | Yes | No | N/A

c. The dollar amounts of transactions for each of the periods for which income statements are presented and the effects of any change in the method of establishing the terms from that used in the preceding period? ___ ___ ___

d. Amounts due from or to related parties as of the date of each balance sheet presented and, if not otherwise apparent, the terms and manner of settlement? ___ ___ ___

[SFAS 57, pars. 2–4]

2. Is information about economic dependency on one or more customers or suppliers disclosed when necessary for a fair presentation? ___ ___ ___
[SFAS 21, par. 9]

3. Is the nature of a controlled relationship disclosed, even though there are no transactions between the enterprises, if the reporting enterprise and one or more other enterprises are under common ownership or management control and the existence of the control could result in operating results or financial position of the reporting enterprise significantly different from those that would have been obtained if the enterprises were autonomous? ___ ___ ___
[SFAS 57, pars. 2 and 4]

Contingencies, Commitments, and Questions About the Entity's Ability to Continue as a Going Concern

1. For loss contingencies, do disclosures indicate:

   a. The nature of the contingency? ___ ___ ___

   b. An estimate of possible loss or range of loss, or a statement that such estimate cannot be made? ___ ___ ___

   [SFAS 5, par. 10]

2. Are the nature and amount of guarantees disclosed (for example, guarantees of indebtedness of others, obligations of banks under standby letters of credit, or guarantees to repurchase receivables that have been sold or otherwise assigned)? ___ ___ ___
[SFAS 5, par. 12; FASBI 34, pars. 1–3]

3. If conditions and events exist that indicate the entity may be unable to continue as a going concern, has consideration been given to the need to disclose:

   a. The principal conditions and events that indicate the going concern problem? ___ ___ ___

   b. Management's evaluation of the significance of these conditions an events? ___ ___ ___

GENERAL (Continued)	Yes	No	N/A
c. The possible effects of such conditions and events, including the possible effects on the recoverability or classification of assets and the amounts or classification of liabilities?	___	___	___
d. Mitigating factors, including management's plans? [SAS 59, par. 11; Interpretation No. 11 of SSARS 1]	___	___	___
4. Is there adequate disclosure of commitments, such as commitments to purchase capital expenditures, inventory purchase agreements, and employment contracts? [SFAS 5, pars. 18–19; ARB 43, Ch. 4, par. 17]	___	___	___
5. Do the financial statements include the following disclosures about risks and uncertainties?			
a. Nature of operations.	___	___	___
b. Use of estimates in the preparation of financial statements.	___	___	___
c. Certain significant estimates (if certain conditions are met.)	___	___	___
d. Current vulnerability due to certain concentrations (if certain conditions are met).	___	___	___
Subsequent Events			
1. Are the financial statements adjusted for any changes in estimates resulting from subsequent events that provide additional evidence about conditions that existed at the date of the statement of assets and liabilities? [SFAS 5, par. 8; SAS 1, secs. 560.03–.04 and .07, and 561.01–.09]	___	___	___
2. Are subsequent events that provide evidence with respect to conditions that did not exist at the date of the balance sheet but arose subsequent to that date adequately disclosed to keep the financial statements from being misleading? [SFAS 5, par. 11; APB 16, par. 61; SAS 1, secs. 560.05–.07 and .09, and 561.01–.09]	___	___	___
Pension Plans — Defined Contribution			
1. Is the following information disclosed about the entity's defined contribution plan:			
a. A description of the plan(s) including employee groups covered, the basis for determining contributions, and the nature and effect of significant matters affecting comparability of information for all periods presented?	___	___	___

GENERAL (Continued)	Yes	No	N/A
b. The amount of cost recognized during the period? [SFAS 87, par. 65]	___	___	___

Limited Liability Companies (LLCs) [PB 14]

	Yes	No	N/A
1. Are the financial statements clearly identified as being those of an LLC?	___	___	___
2. If the LLC has a finite life, do disclosures include the date the LLC will cease to exist?	___	___	___
3. Do disclosures include:			
a. A description of any limitation of an LLC member's liability?	___	___	___
b. The different classes of member's interest and the respective rights, preferences, and privileges of each class?	___	___	___
4. Are all disclosures regarding members' equity and changes in members' equity for the period made?	___	___	___
5. Are all disclosures relating to the conversion of the entity to an LLC made?	___	___	___

STATEMENT OF ASSETS AND LIABILITIES

	Yes	No	N/A
1. For classified balance sheets, are assets and liabilities segregated into current and noncurrent classifications with totals presented for both current assets and current liabilities? [ARB 43, Ch. 3A; SFAS 6, par. 15; FASBI 8, par. 3; TB 79-3]	___	___	___

Cash

	Yes	No	N/A
1. Are restrictions on cash appropriately disclosed? [SFAS 5, pars. 18-19]	___	___	___
2. Is cash that is restricted as to withdrawal or designated for use to acquire noncurrent assets or pay noncurrent debt appropriately segregated from cash available for current operations? [ARB 43, Ch. 3A, par. 6]	___	___	___
3. Are material bank overdrafts presented as liabilities?	___	___	___

STATEMENT OF ASSETS AND LIABILITIES (Continued)

	Yes	No	N/A

Receivables

1. Are other significant types of receivables segregated from normal trade receivables? ___ ___ ___

2. Is the method of accounting for uncollectible accounts disclosed (e.g., the direct write-off or allowance method)? ___ ___ ___

3. If the allowance method is used is the amount of the allowance disclosed? ___ ___ ___

4. If the entity has significant concentrations of credit risk arising from accounts receivable, are the following disclosures provided about each significant concentration (unless the information about the concentration is apparent from the description of the business)?

   a. Information about the activity, region, or economic characteristics that identifies the concentration. ___ ___ ___

   b. The dollar amount of the potential loss if the receivables prove to be of no value. ___ ___ ___

   c. Information about the entity's collateral policies, access to collateral, and a description of the collateral. ___ ___ ___

   [SFAS 105, par. 20]

Inventories

1. Are the major classes of inventory disclosed (e.g., finished goods, work in process, raw materials)? ___ ___ ___
   [ARB 43, Ch. 3A, pars. 4 and 9; ARB 43, Ch. 4, par. 3]

2. Is the method of determining inventory cost (e.g., LIFO, FIFO disclosed)? ___ ___ ___
   [ARB 43, Ch. 3A, par. 9; ARB 43, Ch. 4, pars. 4–16; APB 22, par. 14]

Property and Equipment

1. For depreciable assets, do the financial statements or notes thereto include disclosure of:

   a. Depreciation expense for each period? ___ ___ ___
      [APB 12, par. 5a]

   b. Balances of major classes of depreciable assets by nature or function? ___ ___ ___
      [APB 12, par. 5b]

   c. Accumulated depreciation, either by major classes of assets or in total? ___ ___ ___
      [APB 12, par. 5c]

STATEMENT OF ASSETS AND LIABILITIES (Continued)	Yes	No	N/A
d. The method or methods used in computing depreciation for major classes of depreciable assets? [APB 12, par. 5d; APB 22, par. 14]	___	___	___
2. Are assets that are not used for operations (e.g., idle or held for investment) segregated from other plant and equipment?	___	___	___

Current Liabilities

1. Do current liabilities include the following amounts (appropriately segregated by category)?	___	___	___
a. Accrued liabilities.	___	___	___
b. Collections received in advance of the delivery of goods or performance of services.	___	___	___
c. Other liabilities whose regular and ordinary liquidation is expected to occur within a relatively short time period.	___	___	___
d. Obligations that, by their terms, are due on demand or will be due within one year (or operating cycle, if longer) from the statement of assets and liabilities date.	___	___	___
e. Long-term obligations that because of violations of debt provisions (without appropriate waivers from creditors) cause the obligation to be currently payable on demand, or potentially payable on demand within one year from the statement of assets and liabilities date. [ARB 43, Ch. 1, par. 5; ARB 43, Ch. 3A, pars. 7–8; SFAS 78, par. 5]	___	___	___

Notes Payable and Other Debt

1. Is there adequate disclosure of interest rates, maturities, and other terms and conditions of loan agreements, such as assets pledged as collateral, covenants to restrict debt, maintain working capital, and restrict dividends? [SFAS 5, pars. 18–19]	___	___	___
2. Are the combined aggregate amounts of maturities for all long-term borrowings for each of the five years following the date of the latest balance sheet disclosed? [SFAS 47, par. 10b]	___	___	___
3. Are current portions of debt obligations presented as current liabilities? [ARB 43, Ch. 3A, pars. 7–8]	___	___	___

STATEMENT OF ASSETS AND LIABILITIES (Continued) Yes No N/A

4. If an obligation is excluded from current liabilities because it is expected to be refinanced on a long-term basis, do disclosures include:

   a. A general description of the financing agreement? ___ ___ ___

   b. Terms of any new obligation incurred or expected to be incurred, or equity securities issued or expected to be issued as a result of the refinancing? ___ ___ ___

   [SFAS 6, par. 15; FASBI 8, par. 3; TB 79-3]

Lease Obligations

1. For capital leases, do disclosures include:

   a. Gross amounts of assets recorded by major classes as of the date of each statement of assets and liabilities presented? (These may be combined with owned assets.) ___ ___ ___
   [SFAS 13, par. 16a]

   b. Presentation of lease obligations appropriately segregated by current and long-term portions? ___ ___ ___

   c. Future minimum lease payments as of the latest balance sheet presented in the aggregate and for each of the five succeeding fiscal years with appropriate separate deductions for executory costs and imputed interest to reduce net minimum lease payments to present value? ___ ___ ___
   [SFAS 13, pars. 10 and 16a]

   d. Total of future minimum sublease rentals under noncancelable subleases as of the date of the latest statement of assets and liabilities presented? ___ ___ ___
   [SFAS 13, par. 16a]

   e. Total contingent rentals actually incurred for each period for which an statement of revenue and expenses is presented? ___ ___ ___
   [SFAS 13, par. 16a; SFAS 29, par. 12]

   f. Assets recorded under capital leases and the related accumulated amortization and obligations under the lease identified separately in the statement of assets and liabilities or a note? ___ ___ ___
   [SFAS 13, par. 13]

2. For operating leases that have initial or remaining noncancelable lease terms in excess of one year, do disclosures include:

   a. Future minimum rental payments required as of the latest balance sheet presented in the aggregate and for each of the five succeeding fiscal years? ___ ___ ___

STATEMENT OF ASSETS AND LIABILITIES (Continued) Yes No N/A

b. The total of future minimum rentals under noncancelable subleases as of the date of the latest statement of assets and liabilities presented? ___ ___ ___
[SFAS 13, par. 16b]

3. For all operating leases, do disclosures include rental expense for each period for which an statement of revenue and expenses is presented? ___ ___ ___
[SFAS 13, par. 16c]

4. Do disclosures include a general description of the lessee's leasing arrangements including but not limited to:

   a. Bases for determination of contingent rentals? ___ ___ ___

   b. Terms of any renewal or purchase options or escalation clauses? ___ ___ ___

   c. Restrictive covenants? ___ ___ ___
   [SFAS 13, par. 16d]

Income Taxes

1. Have the types of significant carryforwards been disclosed? ___ ___ ___
[SFAS 109, par. 44]

2. Have the amounts and expiration dates of operating loss and tax credit carryforwards for tax purposes been disclosed? ___ ___ ___
[SFAS 109, par. 48]

3. If the accrual method is used are income taxes for the period accrued? ___ ___ ___

4. Are additional income taxes assessed for prior years accounted for by charging the amount to expense for the current period (if there are no corresponding adjustments to statement of assets and liabilities accounts), or as prior period adjustments? ___ ___ ___

Stockholders' Equity

1. For each class of stock, do disclosures include the number of shares authorized, issued and outstanding, and par or stated value per share? ___ ___ ___

2. Do the financial statements include a description, in summary form, sufficient to explain the pertinent rights and privileges of the various securities outstanding; for example: dividend and liquidation preferences participation rights, buy-sell agreements, and unusual voting rights? ___ ___ ___
[APB 15, par. 19]

3. Are stock option and compensation agreements accounted for properly and adequately disclosed? ___ ___ ___

STATEMENT OF ASSETS AND LIABILITIES (Continued)	Yes	No	N/A
[APB 25, par. 8]			
4. Are changes in the separate component accounts of stockholders' (owners') equity disclosed? [APB 12, par. 10]	___	___	___
5. Are changes in the number of shares of equity securities disclosed? [APB 12, par. 10]	___	___	___
6. If the corporation is an S Corporation, is retained earnings presented as a single amount?	___	___	___

STATEMENT OF REVENUES AND EXPENSES

	Yes	No	N/A
1. Are the important components of income, such as sales, other sources of revenue, cost of sales, selling and administrative expenses, interest expense and income taxes separately disclosed?	___	___	___
2. Is the amount of interest expense disclosed in the statements or notes thereto, and for an accounting period in which some interest cost is capitalized, is the total amount thereof that has been capitalized disclosed? [SFAS 34, par. 21]	___	___	___
3. Are material events or transactions that are unusual in nature or of infrequent occurrence:			
a. Reported as a separate component of income from continuing operations?	___	___	___
b. Accompanied by disclosure of the nature and financial effects of each event? [APB 30, par. 26; TB 82-1, par. 6]	___	___	___

PART II — OTHER DISCLOSURES

INSTRUCTIONS

For topics included in this portion of the disclosure checklist that are *not applicable* (because the entity does not have transactions or accounts related to these topics or the transactions or accounts are immaterial), check "N/A" by the section heading and go to the next section.

	Yes	No	N/A
Accounting Changes and Corrections of Errors			
1. For an accounting change (including one that is expected to have a material effect in the future) does disclosure in the period of the change include:			
a. The nature of the change?	___	___	___
b. Justification for the change?	___	___	___
c. Effect on income? [APB 20, par. 17]	___	___	___
2. Is the correction of an error shown as a prior-period adjustment with disclosure of the following in the period of its discovery and correction:			
a. Nature of the error in previously issued financial statements?	___	___	___
b. Effect of its correction on net income? [APB 20, pars. 36–37; SFAS 16, par. 11]	___	___	___
Business Combinations			
1. If a business combination occurred during the period do the financial statements disclose:			
a. The names and brief description of the acquired or combined companies?	___	___	___
b. Information about any adjustments made to the bases of assets and liabilities?	___	___	___
c. The period for which results of operations of the acquired companies are included in the statement of revenues and expenses?	___	___	___
d. The consideration given?	___	___	___
e. Contingent payments, options, and commitments arising from the combination?	___	___	___
Consolidations			
1. If consolidated statements are presented:			
a. Is the consolidation policy disclosed? [ARB 51, par. 5; APB 22, par. 14]	___	___	___
b. In instances when the financial reporting periods of subsidiaries differ from those of the parent, is recognition given to the effect of interven-			

	Yes	No	N/A
ing events that materially affect financial position or the results of operations? [ARB 51, par. 4; SFAS 12, pars. 18–20; FASBI 14]	___	___	___

Discontinued Operations

1. For discontinued segments of business (actual or planned), do the financial statements disclose:

	Yes	No	N/A
a. Identity of the segment discontinued?	___	___	___
b. Disposal date or expected date of disposal, if known?	___	___	___
c. Manner of disposal or expected manner of disposal?	___	___	___

Financial Instruments with Off-Balance-Sheet Risk

1. For financial instruments with off-balance-sheet risk, are the following disclosures provided?

	Yes	No	N/A
a. The face or contract amount.	___	___	___
b. The nature and terms of the instruments, including credit and market risk, the cash requirements, and the accounting policy.	___	___	___

[SFAS 105, par. 17, as amended by SFAS 119, par. 14]

2. For instruments with off-balance sheet credit risk, are the following disclosures provided?

	Yes	No	N/A
a. The amount of loss the company would incur if any party to the financial instrument failed to perform according to the terms of the contract and the collateral, if any, proved to be of no value.	___	___	___
b. The entity's policy of requiring collateral to support the financial instruments subject to credit risk, its access to the collateral, and a description of it.	___	___	___

[SFAS 105, par. 18, as amended by SFAS 119, par. 14]

Marketable Securities

	Yes	No	N/A
1. Is the aggregate market value of marketable securities disclosed?	___	___	___

	Yes	No	N/A

Nonmonetary Transactions

1. Do disclosures for nonmonetary transactions during the period include:

	Yes	No	N/A
a. Nature of the transactions?	___	___	___
b. Basis of accounting for the assets transferred?	___	___	___
c. Gains or losses recognized on the transfers? [APB 29, par. 28; FASBI 30]	___	___	___

Pension Plans — Defined Benefit

1. Do disclosures include:

	Yes	No	N/A
a. A description of the plan including employee groups covered, type of benefit formula, funding policy, types of assets held and significant nonbenefit liabilities, if any, and the nature and effect of significant matters affecting comparability of information for all periods presented?	___	___	___
b. The amount of net periodic pension cost for the period?	___	___	___

Stock Ownership Plan

If an employer sponsors an employee stock ownership plan (ESOP), do the employer's disclosures include:

	Yes	No	N/A
a. A description of the plan, the basis for determining contributions, including the employee groups covered, and the nature and effect of significant matters affecting comparability of information for all periods presented?			
(1) For leveraged ESOPs and pension reversion ESOPs, the description should include the basis for releasing shares and how dividends on allocated and unallocated shares are used.	___	___	___
b. A description of the accounting policies followed for ESOP transactions, including the method of measuring compensation, the classification of dividends on ESOP shares, and the treatment of ESOP shares for EPS computations?			
(1) If the entity has both old ESOP shares for which it does not adopt the guidance in SOP 93-6 and new ESOP shares for which the guidance in SOP 93-6 is required, are the accounting policies for both blocks of shares disclosed?	___	___	___
c. The amount of compensation cost recognized during the period?	___	___	___

	Yes	No	N/A
d. The number of allocated shares, committed-to-be-released shares, and suspense shares held by the ESOP at the statement of assets and liabilities date?			
(1) If the entity has both old ESOP shares for which it does not adopt the guidance in SOP 93-6 and new ESOP shares for which the guidance in SOP 93-6 is required, is the above disclosure made separately for both blocks of shares?	___	___	___
e. The fair value of unearned ESOP shares at the statement of assets and liabilities date for shares accounted for under SOP 93-6?[1]	___	___	___
f. The existence and nature of any repurchase obligation, including disclosure of the fair value of the shares allocated as of the statement of assets and liabilities date, which are subject to a repurchase obligation?[2] [SOP 93-6, par. 53]	___	___	___

Troubled Debt Restructuring — Debtors

	Yes	No	N/A
1. For troubled debt restructuring occurring during the current period do disclosures include:			
a. A description of the principal changes in terms, the major features of settlement, or both?	___	___	___
b. The aggregate gain on restructuring of payables?	___	___	___
c. The aggregate net gain or loss on transfers of assets recognized during the period? [SFAS 15, par. 25]	___	___	___

[1] This disclosure need not be made for old ESOP shares for which the entity does not apply the guidance in SOP 93-6.

[2] Employers may wish to disclose additional information about the obligation, particularly information about the timing of payments. [SOP 93-6, par. 95]

Appendix A —
SSARS Interpretations

CHAPTER 15

ATTESTATION STANDARDS

Table of Contents

CHAPTER 15

ATTESTATION STANDARDS

Table of Contents (Continued)

CHAPTER 15

ATTESTATION STANDARDS

15.000 INTRODUCTION

15.001 The first Statement on Standards for Attestation Engagements (SSAEs or Attestation Standards) was issued by the AICPA in 1986. Its purpose was to set broad guidelines for engagements in which an accountant expressed assurance on, i.e. attested to, information other than historical financial statements. Since the first statement, four additional statements have been issued pertaining to the following information: (1) financial forecasts and projections, (2) pro forma financial information, (3) internal control structure over financial reporting, and (4) compliance attestation.[1]

Practical Applications

15.002 Although the four SSAEs provide guidance for attesting to specific types of information, many other types of information have been the subject of attestation engagements. Many entities engage accountants to perform services covered by the attestation standards. Although some practitioners may believe these services are requested only by public entities, in today's environment companies of all sizes — both public and nonpublic — are requesting attestation services from their accountants. Therefore, accountants who perform compilation and review services for nonpublic entities should be familiar with the attestation standards to be able to provide their clients with appropriate and useful services. This chapter is intended to provide an overview of attest services and the related standards. Reading this chapter, however, is not sufficient to equip the accountant to perform attest services. Readers should refer to the AICPA's Codification of Statements on Standards for Attestation Engagements for comprehensive guidance on attest services.

15.003 Requests for attest services have grown rapidly over the last decade. This growth has been caused by three major factors. One factor is the need to obtain financing. Information supplied to potential investors and creditors must be credible. Such information has expanded beyond traditional historical financial information, such as financial forecasts, and accountants have been engaged to attest to that information.

---

[1] The first three SSAEs were unnumbered because the Auditing Standards Board (ASB) believed that these statements would be issued infrequently. After three statements were issued, the ASB decided that numbering would facilitate reference to specific standards. They, therefore, codified the first three statements and referred to this codification as SSAE No. 1. The next two statements, pertaining to internal control structure and compliance attestation, were assigned numbers 2 and 3 respectively. The SSAEs are assigned section numbers in the codification — currently AT 100 through AT 500.

15.004 A second factor is marketing products and services. Information supplied to potential customers must also be reliable and accountants have been engaged to attest to that information as well. Examples of such products and services and related attest services include:

- Computer Software — Software developers make assertions about the characteristics of software, such as the speed of certain processing functions, embedded controls, and the content and format of reports. Accountants are engaged to attest to the characteristics asserted by the developers and their reports are made available to potential software purchasers.

- Audience, Circulation Data — Newspapers, magazines, and television and radio stations supply information about audience and circulation to potential advertisers. This information often includes demographic data such as age, educational level, income level, ethnic origin, and religious persuasion, among others. Accountants are engaged to attest to the demographic data provided by the media organizations.

- Occupancy, Attendance, and Enrollment Data — Many entities, such as schools, hotels, hospitals, and charitable organizations provide information about occupancy, attendance, or enrollment. Such information may pertain to the number of students enrolled in a specific program and the dates, location, and attendance pertaining to such programs. Hospitals and hotels may report occupancy data. Accountants are engaged to attest to the data supplied by these entities.

15.005 The third factor is an entity's requirement to comply with specific laws, regulations, or contractual requirements. Many entities are required to report whether they have complied with laws, regulations, or contractual requirements. The recipients of such reports sometimes require that accountants attest to such compliance.

15.006 Illustration 15-1 lists examples of the information or subject matter of various assertions involved in attest engagements in recent years.

ILLUSTRATION 15-1

EXAMPLES OF ATTESTATION ENGAGEMENTS

Subject Matter (Assertion)	Responsible Party (Asserter)
Internal control effectiveness	Financial institutions, government grant recipients, various other entities
Compliance with laws, regulations, and contract terms	Financial institutions, government grant recipients, various other entities
Characteristics of computer software	Software developers
Occupancy, enrollment, and attendance data	Hospitals, hotels, secondary schools, universities, nursing homes
Audience and circulation data	Radio and television stations and networks, newspapers, magazines, and newsletters
Cost justification for utility rate increases	Utility companies
Investment performance statistics — measures of investment performance	Money managers, fund managers
Cost reimbursement data	Health care institutions and government contractors
Labor data for union contract negotiation	Union officials, entity managers, negotiators
Accuracy of grocery prices (market basket of goods)	Grocery stores or chains
Security of automated teller services	Financial institutions and ATM networks
Conceptual and clerical accuracy of textbooks	Textbook publishers

15.100 DEFINITION OF AN ATTEST ENGAGEMENT

15.101 SSAE No. 1 (AT 100.01) defines an attest engagement as follows:

> An attest engagement is one in which an accountant is engaged to issue or does issue a written communication that expresses a conclusion about the reliability of a written assertion that is the responsibility of another party.

This definition contains three key elements: (1) engaged to issue or does issue, (2) written conclusion about reliability, and (3) written assertion that is the responsibility of another party. When all three elements exist in an engagement, the attestation standards apply to that engagement.

Engaged to Issue or Does Issue

15.102 This element sets two conditions under which the standards apply: (1) when the engagement terms indicate that the product of the accountant's engagement is intended to be a level of assurance and (2) the product of the accountant's engagement is a level of assurance, even though it may not have been the original intent.

Written Conclusion About Reliability

15.103 This element means that the accountant issues a written report that provides some level of assurance that certain information conforms to specific criteria. For example, the accountant issues a report expressing an opinion that the design and operation of an entity's internal control structure conforms with specific criteria for effective internal control — such as the COSO report, *Internal Control — Integrated Framework.*[2]

15.104 The attestation standards establish three types of services in which an accountant expresses assurance: (1) examination (audit) engagement, in which an opinion is expressed, (2) review engagement, in which moderate assurance is expressed through negative assurance, and (3) agreed-upon procedures engagement, in which the level of assurance varies with the nature, timing, and extent of procedures performed and negative assurance may or may not be permitted.[3] These services will be discussed in more detail in sections 15.200 - 15.211 in this chapter.

---

[2] The Committee of Sponsoring Organizations of the Treadway Commission (COSO) issued the report, *Internal Control — Integrated Framework*, in 1992. This report has become widely used as a set of criteria for effective internal control.

[3] As discussed in Chapter 1, Sections 1.631-1.639, as this edition of the Manual went to print, the AICPA Auditing Standards Board is issuing two new standards that provide more consistent and comprehensive guidance for agreed-upon procedures engagements. One of these standards is SAS No. 75, *Engagements to Apply Agreed-Upon Procedures to Specified Elements, Accounts or Items of a Financial Statement,* and the other is SSAE No. 4, *Agreed-Upon Procedures Engagements*. Most significantly, the new standards will prohibit the use of negative assurance for all agreed-upon procedures engagements.

Although the new standards are not yet effective—they are effective for reports dated after April 30, 1996—, many of their concepts can be applied currently. Practitioners should be alert to ensure that they comply as the new standards become effective.

Written Assertion That is the Responsibility of Another Party

15.105 This element requires that the information attested to be identified or presented in a statement or report by the party who is responsible for the information. In addition, in that statement or report the responsible party should state that the information conforms to specific criteria.

15.106 The assertion is often the responsibility of the accountant's client. The accountant's attest service adds credibility to the assertion so that other parties may rely on it. In some cases, however, the responsible party may be a group or individual other than the accountant's client. In these situations, the accountant's client desires to rely on the assertion, and the accountant attests to the assertion for the client's benefit. The attestation standards apply in the same manner in either situation.

15.107 The assertion should normally be presented in a report or statement that is separate from the accountant attest report. Only in rare circumstances should the assertion be presented as part of the accountant's report.

15.108 Assertions generally take one of two forms: (1) explicit or (2) implicit. An explicit assertion is a statement by the responsible party that the subject matter of the assertion complies with appropriate criteria. For example, when a responsible party issues a report stating that a presentation of investment performance statistics (the subject matter) complies with standards issued by the Association of Investment Management and Research, this is an explicit assertion.

15.109 An implicit assertion is made when only the subject matter is presented. The most common example is when an entity presents its financial statements. Usually the entity does not make a separate statement that the financial statements conform with GAAP. That assertion is implicit. Another example of an implicit assertion is when an entity presents only its investment performance statistics without an accompanying statement that they conform with a set of criteria. When the assertion is implicit (subject matter only), the presentation of the subject matter should disclose the criteria that are the basis for the presentation.

15.110 In some cases, both an explicit assertion and the subject matter are presented. For example, an entity may present its investment performance statistics and an accompanying statement that the presentation conforms with a specific set of criteria.

Practice Tip:

An accountant cannot at the same time make an assertion and attest to it. AT 100.04 notes that an accountant who has prepared or assisted in preparing an assertion cannot be the asserter but will be considered as the attester. An accountant, however, may assist an entity's management in preparing and supporting a statement or report about some aspect of that entity, such as its internal control structure over financial reporting. Such a service is a consulting engagement. Based on that consulting engagement, management may decide to issue a statement or report about that aspect of the entity, i.e., an assertion. Management may then engage the accountant to perform an attest service and provide assurance about the assertion. The accountant may use work done in the consulting service plus any additional work necessary to comply with the attestation standards and issue an attest report.

15.200 TYPES OF ATTESTATION ENGAGEMENTS

15.201 As noted in 15.104, SSAEs establish three types of attest engagements: examinations, reviews, and agreed-upon procedures.

Examinations

15.202 An examination provides the highest level of assurance on an assertion. It results in the expression of an opinion. Such an engagement is virtually identical to an audit of financial statements under generally accepted auditing standards (GAAS).

15.203 In an examination, the accountant determines the nature, timing, and extent of procedures to apply to the subject matter of the assertion. For example, an accountant may be engaged to audit an assertion about a computer software product. The accountant designs the audit program after considering factors such as the criteria against which the software is to be measured, inherent and control risk, and materiality, among others.

Reviews

15.204 In a review, the accountant provides a moderate level of assurance about the assertion. Often, inquiries and analytical procedures are applied to the subject matter of the assertion to provide such assurance. In such circumstances, reviews under the attestation standards are virtually identical to reviews under Statements on Standards for Accounting and Review Services (SSARS).

15.205 Some assertions and their related subject matter are not susceptible to analytical procedures. For example, in an engagement to review computer software characteristics, the accountant may not be able to design useful analytical procedures. In such cases, accountants often use procedures similar to those that would be used in an examination. However, they vary the nature, timing, and extent of those procedures recognizing that only moderate assurance is needed instead of an opinion.

15.206 Reviews are not permitted for some types of attestation engagements. Specifically, SSAE No. 1, *Financial Forecasts and Projections*, SSAE No. 2, *Reporting on An Entity's Internal Control Structure Over Financial Reporting*, and SSAE No. 3, *Compliance Attestation*, prohibit review engagements for the subject matter they cover.

Practice Tip:

Although the first attestation standard (AT 100) recognized reviews as an acceptable attest service, the tendency of the ASB has been to prohibit them. They are not permitted in attest engagements involving financial forecasts or projections, internal control structure, or compliance with laws and regulations. The authors advise accountants to use caution when accepting a review engagement under the attestation standards, even when they are permitted by professional standards. Such engagements are often difficult to design and often carry a substantial risk of user misunderstanding.

Agreed-Upon Procedures

15.207 An agreed-upon procedures engagement is one in which the three participants, the asserter, the attester, and the report user, agree upon the specific procedures the attester is to apply to the subject matter of the assertion. Such engagements allow the report user to tailor the assurance needed by determining the procedures the accountant is to perform. As a result, the assurance may vary across a broad range, depending on the procedures agreed to. In addition, the specific degree of assurance is inferred by the report user based on the agreed-upon procedures. The attester does not assess the level of assurance conveyed, as in an examination or review.

15.208 In an agreed-upon procedures engagement, the accountant performs the procedures and reports the findings or results of applying them. Such findings or results usually take the form of deviations or discrepancies discovered when the procedures are applied or a statement that no deviations or discrepancies were identified.

15.209 AT 100.59 permits an accountant to express negative assurance in an agreed-upon procedures report. Such assurance states that, based on the procedures applied, nothing other than the findings reported came to the accountant's attention that would cause him or her to believe that the assertion is materially misstated.[4]

15.210 Although AT 100 permits negative assurance for agreed-upon procedures engagements, some subsequent SSAEs have prohibited it for specific attest services. Specifically, SSAE No.2, *Reporting on An Entity's Internal Control Structure Over Financial Reporting,* and SSAE No. 3, *Compliance Attestation,* prohibit negative assurance in agreed-upon procedures engagements.[5]

---

[4] See footnote 3.

[5] See footnote 3.

15.211 Currently, both GAAS and the SSAEs provide guidance about agreed-upon procedures reports. The GAAS guidance is contained in SAS No. 35, *Special Reports—Applying Agreed-upon Procedures to Specified Elements, Accounts, or Items of a Financial Statement* (AU 622) and in SAS No. 75 (with a similar title), which is not yet effective but will supersede SAS No. 35. As the title notes, the SAS guidance should be followed when the accountant is engaged to apply agreed-upon procedures to elements, accounts, or items of an historical financial statement. Examples of elements, accounts or items include accounts receivable, inventory, current assets, expense items, and note disclosures. The SSAEs provide guidance when agreed-upon procedures are applied to subject matter other than historical financial statements.[6]

Practice Tip:

Agreed-upon procedures engagements are discussed in numerous places in professional standards. Illustration 15-2 identifies the specific standards. The nature and extent of the guidance in these various standards varies. (Illustration 15-2 provides the references to these specific standards.) As discussed in Chapter 1, Sections 1.631-1.639, as this edition of the Manual went to print, the AICPA Auditing Standards Board is issuing two new standards that provide more consistent and comprehensive guidance for agreed-upon procedures engagements. One of these standards is SAS No. 75, *Engagements to Apply Agreed-Upon Procedures to Specified Elements, Accounts or Items of a Financial Statement,* and the other is SSAE No. 4, *Agreed-Upon Procedures Engagements.* Most significantly, the new standards will prohibit the use of negative assurance for all agreed-upon procedures engagements.

Although the new standards are not yet effective—they are effective for reports dated after April 30, 1996—, many of their concepts can be applied currently. Practitioners should be alert to ensure that they comply as the new standards become effective.

[6] Ibid.

ILLUSTRATION 15-2

AUTHORITATIVE LITERATURE REFERENCES FOR AGREED-UPON PROCEDURES

Type of Agreed-Upon Procedures Engagement	Authoritative Reference
Agreed-upon procedures applied to elements, accounts, or items in historical financial statements	SAS No. 35, *Special Reports — Applying Agreed-Upon Procedures to Specified Elements, Accounts, or Items of a Financial Statement*
Agreed-upon procedures applied in bank directors' examinations	SOP 90-6, *Directors' Examinations of Banks*
Agreed-upon procedures applied in general attestation engagements and to pro forma financial information	SSAE No. 1 (AT 100 & 300), *Attestation Standards* and *Reporting on Pro Forma Financial Information*
Agreed-upon procedures applied to financial forecasts and projections	SSAE No. 1 (AT 200), *Financial Forecasts and Projections*
Agreed-upon procedures applied to internal control structure over financial reporting	SSAE No. 2, *Reporting on an Entity's Internal Control Structure Over Financial Reporting*
Agreed-upon procedures applied to compliance with laws and regulations	SSAE No. 3, *Compliance Attestation*
NOTE: SAS No. 75, which is being issued as this edition of the manual went to print, will supersede SAS No. 35. SSAE No. 4, which is being issued in conjunction with SAS No. 75, will supersede and amend some paragraphs of SSAE Nos. 1 to 3. Both of the new standards will be effective for reports dated after April 30, 1996. Refer to footnote 3 of this chapter for more information.	

15.300 OVERVIEW OF ATTESTATION STANDARDS

15.301 AT 100 establishes eleven attestation standards. These standards are similar to the ten generally accepted auditing standards and are organized into the identical categories of (1) general standards, (2) fieldwork standards, and (3) reporting standards.

General Standards

15.302 The first general standard requires accountants who perform attest services to be proficient in attestation. Ordinarily, an accountant who is qualified to perform financial statement audits is qualified to perform attest services. These qualifications include a license to practice public accounting and adequate experience in auditing. Accountants should be aware, however, that the evidence gathering and evaluation aspects of attestation may require special training or experience in some attest engagements.

15.303 The second general standard requires accountants to have adequate knowledge of the subject matter of the assertion. Given the wide variety of subject matter that may be attested to, accountants should ensure that they have sufficient knowledge of the subject matter to assess inherent and control risks relevant to it, determine the evidence to be obtained, design tests to gather that evidence, evaluate the evidence, and report the conclusions.

15.304 The second general standard recognizes that accountants may require assistance from specialists about certain subject matter. Thus, similar to use of specialists in a financial statement audit, specialists may be used in attestation engagements to fulfill the subject matter expertise requirements.

15.305 The third general standard establishes requirements concerning the criteria used by the responsible party (asserter) to prepare the assertion. Criteria are the standards that determine whether the subject matter is appropriate. For example an assertion that an entity's internal control structure over financial reporting is properly designed and operating effectively, requires standards or criteria to judge whether such an assertion is appropriate. Similarly, an assertion that an entity has complied with certain aspects of specific laws or regulations requires standards or criteria by which to judge compliance.

15.306 The third general standard sets two conditions concerning criteria. First, the criteria must be reasonable. Reasonableness is determined by the accountant's judgment. The third standard, however, provides guidance to assist accountants in judging reasonableness. Criteria established by a body designated by AICPA's Council under the AICPA Code of Professional Conduct are considered reasonable by definition. Criteria established by other bodies, such as regulators and industry associations, that follow due process are also considered to meet the reasonableness test. Criteria established by bodies that do not follow due process, however, should be evaluated and, if determined to be reasonable, the criteria should be included in the presentation of the assertion or related subject matter.

15.307 Criteria may be agreed-upon among the asserter, the attester, and the report user(s). Such criteria is deemed to be reasonable for these parties when agreed upon. The accountant's attest report, however, must be restricted to these parties, since the criteria are not necessarily suitable for general distribution.

15.308 The second condition pertains to the objectivity of the assertion. An assertion cannot be so subjective that accountants using the same criteria would likely arrive at substantially different conclusions about the appropriateness of the assertion. For example, an accountant should not attest to an assertion that an entity has the "best" software, or the "most effective" internal control in the industry.

Practice Tip:

The objectivity of criteria is often a troublesome practice problem. Accountants should be satisfied that they can measure conformity with the criteria in an objective manner before they undertake an attest engagement. For example, if an assertion is made that cash receipts are deposited on a timely basis, the accountant should require that "timely" be defined in a measurable manner, such as within 3 business days of receipt. An accountant should be wary of using his or her judgment to interpret criteria. This amounts to setting the criteria, which is an inappropriate role for the accountant in an attest engagement.

15.309 The fourth general standard requires independence in attestation engagements. Independence for attest services is defined in the AICPA Code of Professional Conduct (see section ET 101.13), and is virtually the same as for audit services under GAAS. There is one difference, however, that accountants should be aware of. In an attest engagement, only the attest team needs to be independent — not the firm. The basis for creating this difference is that attest engagements are ordinarily considered to be nonrecurring engagements. Thus, the AICPA did not believe it necessary to require the entire accounting firm to be independent, as in a financial statement audit.

Practice Tip:

At the time this edition of the Manual was printed, the AICPA's Professional Ethics Committee was developing a modification of the attest independence rules. This modification would require firm independence for some, if not all, attest engagements. To determine the current status of ethics rules for such engagements, call the Professional Ethics division at 800-862-4272, menu option 4.

15.310 The fifth general standard establishes a requirement to exercise due care in an attest engagement. The due care standard, in attest as in audit engagements, is a broad standard requiring reasonable care and diligence in performing professional services involving attestation.

Fieldwork Standards

15.311 There are two attestation fieldwork standards. The first requires that work be adequately planned and assistants properly supervised. The second requires that sufficient evidence be obtained to support the attest conclusion expressed in the report.

15.312 Both of the attestation fieldwork standards are virtually identical to their counterparts in the GAAS fieldwork standards. Implementing these standards in an attest engagement involves the same considerations as in an engagement to audit or review financial statements.

Reporting Standards

15.313 The four attestation reporting standards parallel the reporting standards in GAAS. The first standard requires that the accountant's report identify the assertion reported on and state the character of the engagement. Meeting this standard simply requires that the accountant's report refer to management's assertion and state the nature of the attest service — examination, review, or agreed-upon procedures. Illustrative attest reports are shown in sections 15.402 through 15.404.

15.314 The second reporting standard requires that the accountant's report express a conclusion about whether the assertion conforms with the criteria against which it was measured. This requirement is similar to the GAAS requirement for the accountant to state whether the financial statements (assertion) conform with GAAP (criteria). In an attest engagement involving the internal control structure, for example, the accountant would state whether the assertion that the internal control structure is effective conforms with appropriate criteria, such as the COSO report.

15.315 The third reporting standard requires the accountant to report any material departures from the relevant criteria and any material scope limitations. Departures from criteria in an examination engagement can result in either a qualified opinion or an adverse opinion, depending on materiality. In a review engagement, uncorrected departures from criteria should be disclosed in the review report.

15.316 Scope limitations in an examination engagement can result in either a qualified opinion or a disclaimer of opinion, depending on the significance of the scope limitations. In a review engagement, scope limitations ordinarily require that the accountant withdraw from the engagement.

15.317 The fourth reporting standard concerns engagements that involve either agreed-upon procedures or agreed-upon criteria. In either type of engagement, the report should be restricted to the parties involved in the agreements. Distribution to other parties may result in misleading conclusions.

Documentation Guidance

15.318 Documentation guidance is evolving in the SSAEs. Currently, none of the SSAEs contain workpaper documentation requirements. The authors recommend that accountants follow applicable GAAS and SSARS guidance for workpaper documentation in attestation engagements.[7]

15.319 SSAE No. 3, *Compliance Attestation*, (AT 500.70) requires that accountants obtain a representation letter from the asserter in both agreed-upon procedures and examination engagements. AT 500.70 specifies nine representations the asserter should include in the representation letter. An illustrative representation letter that meets the requirements of AT 500.70 is contained in section 15.405 of this Chapter. Accountants, however, should also consult AT 500.70 when preparing representation letters in SSAE No. 3 engagements.

15.320 The SSAEs, like GAAS, do not require engagement letters. The authors recommend, however, that accountants use engagement letters in all attestation engagements to help achieve and document an understanding of the services the accountant is to provide. Illustrative engagement letters are contained in sections 15.406 and 15.407 of this Chapter.

[7] As this edition of the Manual went to print, the AICPA Auditing Standards Board is expected to soon issue an SAS and an SSAE that will provide guidance on workpapers for attestation engagements. The proposed statements, *Omnibus Statement on Auditing Standards-1995* and *Omnibus Statement on Standards for Attestation Engagements-1995*, were released in February 1995 and are expected to be issued in final form in December 1995. The statements amend several pronouncements. In particular, SSAE No. 1 (AT 100) is amended to require practitioners to prepare and maintain workpapers in connection with an attestation engagement. The amendment is proposed to be effective for engagements beginning after December 15, 1995.

15.400 DOCUMENTATION ASSISTANCE

15.401 The following sections show illustrative letters and reports for various attestation engagements.

15.402 Attestation Report — Examination Service

Independent Accountant's Report[8]

____
____
____

I (We) have examined the accompanying (identify the presentation of assertions — for example Statement of Performance and Operating Characteristics of GAAPWise Software, Version 3.0 as of June 30, 19XX). My (Our) examination was made in accordance with standards established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as I (we) considered necessary in the circumstances.

(Additional paragraphs may be added to emphasize certain matters related to the attest engagement or the presentation of assertions.)

In my (our) opinion, the (identify the presentation of assertions — for example Statement of Performance and Operating Characteristics) referred to above presents (identify the assertion — for example the performance and operating features of GAAPWise Software, Version 3.0, as of June 30, 19XX) in conformity with (identify established or stated criteria — for example, the measurement and disclosure criteria set forth in Note X).

[Signature]

[Date][9]

---

[8] A title is not required when performing attest engagements under sections AT 100, AT 200 and AT 300. Sections AT 400 (internal control structure over financial reporting) and AT 500 (compliance attestation) require a title that contains the word "independent." The authors recommend using a title that contains the word "independent" in all attestation reports.

[9] Report should be dated as of the completion of fieldwork.

15.403 Attestation Report — Review Service

Independent Accountant's Report[10]

____
____
____

I (We) have reviewed the accompanying (identify the presentation of assertions — for example Statement of Performance and Operating Characteristics of GAAPWise Software, Version 3.0 as of June 30, 19XX). My (Our) review was conducted in accordance with standards established by the American Institute of Certified Public Accountants.

A review is substantially less in scope than an examination, the objective of which is the expression of an opinion on (identify the presentation of assertions — for example Statement of Performance and Operating Characteristics of GAAPWise Software, Version 3.0 as of June 30, 19XX). Accordingly, I (we) do not express such an opinion.

(Additional paragraph(s) may be added to emphasize certain matters related to the attest engagement or the presentation of assertions.)

Based on my (our) review, nothing came to my (our) attention that caused me (us) to believe that the accompanying (identify the presentation of assertions — for example, Statement of Performance and Operating Characteristics of GAAPWise Software, Version 3.0 as of June 30, 19XX) is not presented in conformity with (identify established or stated criteria — for example, the measurement and disclosure criteria set forth in Note 15).

[Signature]

[Date]

---

[10] Review reports are permitted only for attest services performed under sections AT 100 and AT 300 (general attest engagements and pro forma financial information, respectively). Neither section requires that review reports contain a title. The authors recommend that review reports issued under either sections AT 100 or AT 300 include a title that contains the word "independent."

15.404 Attestation Report — Agreed-Upon Procedures Report [11]

Independent Accountant's Report

____
____
____

I (We) have applied the procedures enumerated below to the accompanying (identify the presentation of assertions — for example Statement of Performance and Operating Characteristics of GAAPWise Software, Version 3.0 as of June 30, 19XX). These procedures, which were agreed to by ABC Inc. and XYZ Co., were performed solely to assist you in evaluating (identify the assertion — for example the performance and operating features of GAAPWise Software, Version 3.0, as of June 30, 19XX). This report is intended solely for your information and should not be used by those who did not participate in determining the procedures.

(Include paragraph to enumerate procedures and findings or to refer to them.)

These agreed-upon procedures are substantially less in scope than an examination, the objective of which is the expression of an opinion on (identify the presentation of assertions — for example Statement of Performance and Operating Characteristics of GAAPWise Software, Version 3.0 as of June 30, 19XX). Accordingly, I (we) do not express such an opinion.

Based on the application of the procedures referred to above, nothing came to my (our) attention that caused me (us) to believe that the accompanying (identify the presentation of assertions — for example, Statement of Performance and Operating Characteristics of GAAPWise Software, Version 3.0 as of June 30, 19XX) is not in conformity with (identify the established, stated, or agreed-upon criteria — for example, the measurement and disclosure criteria set forth in Note X). Had I (we) performed additional procedures or had I (we) made an examination of the (identify the presentation assertions — for example, Statement of Performance and Operating Characteristics), other matters might have come to my (our) attention that would have been reported to you.

[Signature]

[Date]

---

[11] Reporting requirements for agreed-upon procedures engagements vary among specific attestation standards. For example, only section AT 500 requires a title for an agreed-upon procedures report that includes the word "independent." The authors recommend, however, that such a title be used in all agreed-upon procedures reports. In addition, sections AT 100, AT 200, and AT 300 permit expressions of negative assurance in agreed-upon procedures reports. Sections AT 400 and AT 500 do not permit negative assurance. However, as discussed in Chapter 1, Sections 1.631-1.639, as this edition of the Manual went to print, the Auditing Standards Board is issuing SAS No. 75 and SSAE No. 4 that will, among other things, prohibit the use of negative assurance for all agreed-upon procedure engagements. The SAS and the SSAE will be effective for reports dated after April 30, 1996. Practitioners issuing reports after this date should consult the new pronouncements for illustrative reports.

15.405 Attestation Engagement Representation Letter—Examination or Agreed-Upon Procedures Engagement

[To the Accountant]

In connection with your (examination of or application of agreed-upon procedures to) [name of entity]'s compliance with [list specified compliance requirements] during the [period] ended [date] included in the accompanying [title of management report], we confirm, to the best of our knowledge and belief, the following representations made to you during your engagement.

1. We acknowledge that we are responsible for complying with the [list specified compliance requirements].
2. We acknowledge that we are responsible for establishing and maintaining an effective internal control structure of compliance with the compliance requirements noted in item 1 above.
3. We have performed an evaluation of the entity's compliance with the requirements noted in item 1 above.
4. We are in compliance with the requirements noted in item 1 above, based on [identify compliance criteria].
5. We have disclosed to you all known noncompliance with the requirements noted in item 1 above.
6. We have made available to you all documentation related to compliance with the specified requirements noted in item 1 above.
7. We have interpreted compliance with [state specific compliance requirement(s)] to mean [state management's interpretation of any compliance requirements that have varying interpretations].
8. We have disclosed to you all communications from regulatory agencies, internal auditors, and other practitioners concerning possible noncompliance with the specified requirements noted in item 1 above, including communications received between the end of the period addressed in our assertion and the date of your report.
9. We have disclosed to you any known compliance occurring subsequent to the period for which, date as of which, we have made our assertion.

____
[Signature of Owner or Chief Executive Officer]

____
[Date]

____
[Signature of Chief Financial Officer, if applicable]

____
[Date]

15.406 Engagement Letter — Examination Engagement Under SSAEs

____
____
____

This letter is confirm my (our) understanding of the terms and objectives of my (our) engagement and the nature and limitations of the services I (we) will provide.

- I (We) will examine (name of entity)'s assertions with (list specified assertions) during the (period) ended (date) in accordance with standards established by the American Institute of Certified Public Accountants and will include such tests and other examination procedures as we consider necessary in the circumstances.

My (Our) report is expected to read as follows:

> I (We) have examined the accompanying (identify the presentation of assertions — for example Statement of Performance and Operating Characteristics of GAAPWise Software, Version 3.0 as of June 30, 19XX). My (Our) examination was made in accordance with standards established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as I (we) considered necessary in the circumstances.
>
> (Additional paragraphs may be added to emphasize certain matters related to the attest engagement or the presentation of assertions.)
>
> In my (our) opinion, the (identify the presentation of assertions — for example Statement of Performance and Operating Characteristics) referred to above presents (identify the assertion — for example the performance and operating features of GAAPWise Software, Version 3.0, as of June 30, 19XX) in conformity with (identify established or stated criteria — for example, the measurement and disclosure criteria set forth in Note X).

At the completion of my (our) examination, I (we) will request that you sign a letter acknowledging your responsibility for the assertions and other matters related to it.

My (Our) fees will be billed as work progresses and are based on the amount of time required plus out-of-pocket expenses. Invoices are payable upon presentation. I (We) will notify you immediately of any circumstances I (we) encounter that could significantly affect my (our) initial estimate of total fees, which will range from $_________ to $_________.

If this letter correctly expresses your understanding, please sign the enclosed copy where indicated and return it to me (us).

I (We) appreciate the opportunity to serve you and trust that our association will be a long and pleasant one.

Sincerely,

____
[Engagement Partner's Signature]

____
[Date]

Accepted and agreed to:

____
[Client Representative's Signature]

____
[Title]

____
[Date]

15.407 Engagement Letter — Agreed-Upon Procedures Engagement Under SSAEs

____
____
____

This letter is confirm my (our) understanding of the terms and objectives of my (our) engagement and the nature and limitations of the services I (we) will provide.

- I (We) will apply the agreed-upon procedures listed in the accompanying schedule to (name of entity)'s compliance with (list specified compliance requirements) during the (period) ended (date) in accordance with standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of [name specified users of report]. Consequently, we make no representations as to the sufficiency of these procedures. This engagement is solely to assist (name users) in (describe nature of engagement). If, for any reason, I (we) are unable to complete the procedures, we will not issue a report as a result of our engagement.
- I (We) will issue a report listing the procedures performed and the findings resulting from those procedures. This report is solely for the use of [name specified users] and should not be used by any other parties. Because the procedures listed in the attached schedule do not constitute an audit, I (we) will not express an opinion on [name of entity]'s compliance with the specified requirements noted above. Our report will contain a paragraph indicating that had we performed additional procedures or an audit, other matters might have come to our attention that would have been reported to you.

Compliance with the specified requirements listed above is (name of responsible party)'s responsibility. At the completion of my (our) examination, I (we) will request that you sign a letter acknowledging this responsibility and other matters related to it.

My (Our) fees will be billed as work progresses and are based on the amount of time required plus out-of-pocket expenses. Invoices are payable upon presentation. I (We) will notify you immediately of any circumstances I (we) encounter that could significantly affect my (our) initial estimate of total fees, which will range from $__________ to $__________.

If this letter correctly expresses your understanding, please sign the enclosed copy where indicated and return it to me (us).

I (We) appreciate the opportunity to serve you and trust that our association will be a long and pleasant one.

Sincerely,

____
[Engagement Partner's Signature]

____
[Date]

Accepted and agreed to:

____
[Client Representative's Signature]

____
[Title]

____
[Date]

Appendix B —
Qs and As

AR Section

STATEMENTS ON STANDARDS FOR ACCOUNTING AND REVIEW SERVICES

Statements on Standards for Accounting and Review Services are issued by the AICPA Accounting and Review Services Committee, the senior technical committee of the Institute designated to issue pronouncements in connection with the unaudited financial statements or other unaudited financial information of a nonpublic entity. Council has designated the AICPA Accounting and Review Services Committee as a body to establish technical standards under Rule 202 of the Institute's Code of Professional Conduct.

The staff of the Accounting and Review Services Committee has been authorized to issue interpretations to provide timely guidance on the application of pronouncements of the accounting and review services committee. Interpretations are reviewed by members of that committee. An interpretation is not as authoritative as a pronouncement of the Accounting and Review Services Committee, but members should be aware that they may have to justify a departure from an interpretation if the quality of their work is questioned.

TABLE OF CONTENTS

AR Section 9100

Compilation and Review of Financial Statements: Accounting and Review Services Interpretations of Section 100

1. Omission of Disclosures in Reviewed Financial Statements

.01 *Question*—Section 100.19—.21, *Compilation and Review of Financial Statements,* provides guidance to the accountant when a departure from generally accepted accounting principles relates to the omission of substantially all disclosures in the financial statements that he has compiled. Section 100.39 states that, in all other circumstances, an accountant should consider whether modification of his standard report is adequate to disclose a departure from generally accepted accounting principles. When a departure from generally accepted accounting principles relates to the omission of substantially all disclosures in financial statements that the accountant has reviewed, is disclosure of such omission in a separate paragraph of the accountant's report similar to the example in section 100.21 an adequate modification of his report?

.02 *Interpretation*—No. The guidance in section 100.19—.21 only applies when financial statements that the accountant has *compiled* omit substantially all of the disclosures required by generally accepted accounting principles or another comprehensive basis of accounting. Because of the reporting requirements of section 100, an accountant ordinarily would not accept an engagement to review financial statements that omit substantially all of the disclosures required by generally accepted accounting principles. When an accountant who undertakes to *review* financial statements subsequently finds that his client declines to include substantially all required disclosures, his review report should include the disclosures omitted from the statements. However, if the information required to be disclosed has not been determined by management or is not known as the result of the accountant's procedures, the accountant is not required to determine the specific information that should be disclosed. In that circumstance, the accountant's report should specifically identify the nature of the omitted disclosures.

[Issue Date: December, 1979.]

2. Financial Statements Included in SEC Filings

.03 *Question*—Statements on Standards for Accounting and Review Services are applicable to the unaudited financial statements or other unaudited financial information of nonpublic entities (see definition in section 100.04, as amended by section 200.01, footnote 2). Unaudited financial statements of some entities that are nonpublic are occasionally included in documents filed with the Securities and Exchange Commission. For example, a nonpublic entity may be required to file unaudited financial statements in connection with the issuance of stock to an employee stock purchase plan or in connection with the sale of certain limited partnership units. Do the reporting requirements of section 100 apply in those circumstances?

.04 *Interpretation*—Deciding whether an entity is public or nonpublic for purposes of determining the applicability of section 100 should involve consideration of all relevant facts and the application of professional judgment. Professional standards do not eliminate the need for the exercise of professional judgment, since rules and definitions, no matter how carefully drawn, seldom cover every eventuality.

.05 In the circumstances described in this question, the accountant might note that the definition of a nonpublic entity contained in section 100, developed from the definition of a publicly traded company in APB Opinion No. 28 [AC section I73.101], differs from the definition of a nonpublic enterprise in FASB Statement No. 21 [AC section S20.407], which excludes any entity "that is required to file financial statements with the Securities and Exchange Commission." This might lead the accountant to consider the significant responsibilities placed on independent accountants by the various securities acts. He might conclude that the users of unaudited financial statements included in documents filed with the SEC have objectives, needs, and expectations different from those of users of the unaudited financial statements of nonpublic entities that are not included in such filings. He might also conclude that communication with those users, because of the significance they attach to the regulatory and disciplinary responsibilities of the SEC, is not enhanced by including a compilation or review report in a document filed with the SEC, and might responsibly decide that the guidance in Statements on Auditing Standards is more appropriate in those circumstances.

[Issue Date: December, 1979.]

3. Reporting on the Highest Level of Service

.06 *Question*—Sections 100.04 and 100.11, *Compilation and Review of Financial Statements,* recognize that an accountant may consider it necessary to perform other accounting services to enable him to compile financial statements. Section 100.05 provides that when an accountant performs more than one service with respect to the financial statements of an entity he should issue the report that is appropriate for the highest level of service rendered. Does section 100.05 require the accountant to evaluate the extent of other accounting services he has performed in a compilation engagement and to decide whether a review report should be issued instead of a compilation report?

.07 *Interpretation*—No. Section 100 requires the accountant to issue a report whenever he completes a compilation or review of the financial statements of a nonpublic entity. The statement that the accountant should issue a report that is appropriate for the highest level of service rendered is intended to make clear that if, for example, the accountant has both compiled and reviewed the financial statements that he was engaged to review, he would need to issue only a review report.

.08 Section 100 imposes no requirement for the accountant to "upgrade" his report because he has performed other accounting services. However, the accountant may wish to evaluate whether, as a result of performing such services, he is in a position to issue a review report when he was engaged only to perform a compilation. In such circumstances, he may wish to discuss the matter with his client and they may decide to revise their understanding regarding the nature of the services to be rendered.

.09 *Question*—An entity may wish to engage an accountant to compile financial statements each month and also to review the financial statements of the entity for a quarterly or an annual period. May an accountant issue a compilation report on the monthly financial statements and a review report on quarterly or annual financial statements for a period ending on the same date as one of the monthly financial statements?

.10 *Interpretation*—Yes. An accountant may accept an engagement to perform a compilation of financial statements for an interim period and an engagement to review the financial statements for another period that ends on the same date, provided he complies with the applicable standards for each engagement.

.11 *Question*—An accountant who has been engaged to compile or review the financial statements of an entity may also be requested to perform a higher level of service with respect to the same financial statements. Is the acceptance of such an engagement appropriate?

.12 *Interpretation*—Yes. Section 100 does not prohibit the accountant from accepting an engagement to perform a higher level of service with respect to financial statements that have been previously compiled or reviewed.

[Issue Date: December, 1979.]

4. Discovery of Information After the Date of the Accountant's Report

.13 *Question*—Paragraph 42 of SSARS 1 [section 100.42], *Compilation and Review of Financial Statements,* states that the accountant may wish to consider the guidance in section 561 of Statement on Auditing Standards No. 1 [AU section 561] in determining an appropriate course of action when he becomes aware, subsequent to the date of his report on compiled or reviewed financial statements, that facts may have existed at that date which might have caused him to believe that information supplied by the entity was incorrect, incomplete, or otherwise unsatisfactory had he then been aware of such facts. What factors would the accountant ordinarily consider in determining an appropriate course of action and how would his judgments be affected by the nature of the service he had provided?

.14 *Interpretation*—Determining an appropriate course of action in the circumstances addressed in paragraph 42 of SSARS 1 [section 100.42] requires the careful exercise of professional judgment. Two factors that the accountant might consider in making this decision are:

(a) *The reliability of the information.* If the information is of such a nature and from such a source that the accountant would have obtained additional or revised information during the course of his compilation or performed additional procedures during the course of his review, the accountant ordinarily would discuss the information with his client and consider the results of that discussion in determining what other action, if any, to take. The nature and extent of any procedures applied by the accountant relative to the reliability of the information would be similar to those that he would have applied had he become aware of the information during the course of his engagement. If the accountant believes that the information is reliable and that it existed at the date of his report, and if the information indicates that the financial statements, his report, or both need revision, the accountant ordinarily would conclude that persons known to be relying on or likely to rely on the financial statements should be notified in an appropriate manner.

(b) *The existence of persons known to be relying on or likely to rely on the financial statements.* The compiled or reviewed financial statements of nonpublic entities may be distributed to persons who are not otherwise informed about the entity's financial position, results of operations, and cash flows. In evaluating the likelihood that such persons are currently relying on or likely to rely on the financial statements, the accountant should consider the time elapsed since the financial statements were issued. Although a compilation report does not express any form of assurance on the financial statements, it would seldom be appropriate for an accountant to conclude, simply because his responsibilities were limited to a compilation service, that notification of third party users in the absence of notification by the client is not required when the accountant knows that the financial statements should be revised.

.15 As indicated in both paragraph 42 of SSARS 1 [section 100.42] and, more explicitly, in section 561.02 of SAS No. 1 [AU section 561.02], the accountant should consider consulting with his attorney.

[Issue Date: November, 1980.]

5. Planning and Supervision

.16 *Question*—SSARS 1 [section 100], *Compilation and Review of Financial Statements,* states that it "provides guidance considered necessary to enable the accountant to comply with the general standards of the profession set forth in the AICPA Code of Professional Conduct." Rule 201C [ET section 201.01C] states: "Adequately plan and supervise the performance of professional services." Although Statement on Auditing Standards No. 22 [AU section 311], *Planning and Supervision,* deals with these matters in the context of an audit in accordance with generally accepted auditing standards, SSARS 1 [section 100] does not provide specific guidance for the planning and supervision of a compilation or review engagement. In the absence of specific guidance on planning and supervision in SSARS 1 [section 100], is an accountant required to follow the guidance provided in SAS No. 22 [AU section 311] in the context of a compilation or review engagement for a nonpublic entity?

.17 *Interpretation*—No. Statements on Auditing Standards do not govern engagements to compile or review financial statements of a nonpublic entity. However, an accountant may wish to consider SAS No. 22 [AU section 311] or other reference sources, such as textbooks and articles, when he needs additional information on planning and supervision.

[Approved: May, 1981; Issue Date: August, 1981.]

6. Withdrawal From Compilation or Review Engagement

.18 *Question*—Paragraph 41 of SSARS 1 [section 100.41] states: "If the accountant believes that modification of his standard report is not adequate to indicate the deficiencies in the financial statements taken as a whole, he should withdraw from the compilation or review engagement and provide no further services with respect to those financial statements." Under what circumstances would the accountant ordinarily conclude that it is necessary to withdraw from a compilation or review engagement?

.19 *Interpretation*—Modification of the accountant's standard report as described in paragraph 40 of SSARS 1 [section 100.40] ordinarily should be adequate to indicate the deficiencies in the financial statements taken as a whole. However, in some circumstances, likely to be rare and unusual, the nature, extent, and probable effect of the departures from generally accepted accounting principles or an other comprehensive basis of accounting might cause the accountant to question whether the departures were undertaken with the intention of misleading those who might reasonably be expected to use such financial statements. In those circumstances, withdrawal from the compilation or review engagement might be necessary; however, the accountant ordinarily would not make a decision to withdraw when the client agreed that the effects of the departures should be determined and disclosed in the accountant's report.

.20 As an illustration, the client may have entered into a number of leasing arrangements that might be required to be capitalized under FASB Statement No. 13 [AC section L10]. The client may not wish to capitalize such leases and may not have determined the effect of this departure from GAAP. However, the client may be willing to disclose in the financial statements information such as the nature of the leased property, the payments required under the leases, and other important terms of the leases. In those circumstances, the accountant is not likely to conclude that the departure was undertaken with the intention of misleading users, even though the effect of the departure is not quantified in the financial statements or the accountant's report.

.21 On the other hand, the client may have failed, for example, to make provision for doubtful accounts and probable sales returns in the face of significant adverse business and economic conditions and may be unwilling to acknowledge that an adjustment should be considered. This might cause the accountant to question whether other information provided by the client is incorrect, incomplete, or otherwise unsatisfactory. Also, the accountant's general knowledge of the entity's business and related matters might lead him to conclude that this position indicates an intention of misleading users, particularly if the effects of the departure are not determined.

.22 The accountant would also withdraw from the compilation or review engagement when the financial statements, including disclosures, are not revised and the client refuses to accept the modified standard report that the accountant believes is appropriate.

[Approved: May, 1981; Issue Date: August, 1981.]

7. Reporting When There are Significant Departures From Generally Accepted Accounting Principles

.23 *Question*—When the financial statements include significant departures from generally accepted accounting principles or an other comprehensive basis of accounting, may the accountant modify his standard report under paragraph 40 of SSARS 1 [section 100.40] to include a statement that the financial statements are not in conformity with generally accepted accounting principles or an other comprehensive basis of accounting?

.24 *Interpretation*—No. Including such a statement in the accountant's compilation or review report would be tantamount to expressing an adverse opinion on the financial statements taken as a whole. Such an opinion can be expressed only in the context of an audit engagement. Furthermore, such a statement in a review report would confuse users because it would contradict the expression of limited assurance required by paragraph 32(e) of SSARS 1 [section 100.32(e)].

.25 However, footnote 18 to paragraph 40 of SSARS 1 [section 100.40, footnote 18] indicates that the accountant is not precluded from emphasizing in a separate paragraph of his report a matter regarding the financial statements. The accountant may wish, therefore, to emphasize the limitations of the financial statements in a separate paragraph of his compilation or review report, depending on his assessment of the possible dollar magnitude of the effects of the departures, the significance of the affected items to the entity, the pervasiveness and overall impact of the misstatements, and whether disclosure has been made of the effects of the departures. Such separate paragraph, which would follow the other modifications of his report (see illustrations in paragraph 40 of SSARS 1 [section 100.40]), might read as follows:

> Because the significance and pervasiveness of the matters discussed above makes it difficult to assess their impact on the financial statements taken as a whole, users of these financial statements should recognize that they might reach different conclusions about the company's financial position, results of operations, and cash flows if they had access to revised financial statements prepared in conformity with generally accepted accounting principles.

.26 Inclusion of such a separate paragraph in the accountant's compilation or review report is not a substitute for disclosure of the specific departures or the effects of such departures when they have been determined by management or are known as a result of the accountant's procedures. In this connection, see the interpretation entitled "Omission of Disclosures in Reviewed Financial Statements" (section 9100.01-.02).

[Approved: May, 1981; Issue Date: August, 1981.]

8. Reports on Specified Elements, Accounts, or Items of a Financial Statement

.27 *Question*—Paragraph 43 of SSARS 1 [section 100.43] provides guidance when the basic financial statements are accompanied by information presented for supplementary analysis purposes. However, a nonpublic entity may wish to engage an accountant to issue a review report on a separate presentation of specified elements, accounts, or items of a financial statement or to report the results of applying agreed-upon procedures to specified elements, accounts, or items of a financial statement. Do SSARS 1 [section 100] reporting requirements for a review apply in such circumstances?

.28 *Interpretation*—No. SSARS 1 [section 100], *Compilation and Review of Financial Statements,* provides guidance concerning the standards and procedures applicable to compilations and reviews of financial statements. Presentations of specified elements, accounts, or items of a financial statement are not financial statements. Statement on Auditing Standards (SAS) No. 62 [AU section 623] and Interpretations thereof provide guidance with respect to reporting on such presentations when the engagement is intended to result in the expression of an audit opinion. SAS No. 35 [AU section 622] provides guidance with respect to reporting on the results of applying agreed-upon procedures to specified elements, accounts, or items of a financial statement. Statements on Standards for Attestation Engagements, *Attestation Standards* [AT section 100], provides guidance with respect to reporting on such presentations when the accountant is engaged to express moderate assurance in a review report.

[Issue Date: November, 1981.]

9. Reporting When Management Has Elected to Omit Substantially All Disclosures

.29 *Question*—Paragraph 21 of SSARS 1 [section 100.21] illustrates a form of standard report appropriate when compiled financial statements omit substantially all disclosures. The third paragraph of that illustrative report begins with this sentence: "Management has elected to omit substantially all of the disclosures . . . required by generally accepted accounting principles." Paragraph 19 of SSARS 1 [section 100.19] requires the accountant to disclose in his report the fact that compiled financial statements omit substantially all disclosures but does not state that there is a need to indicate that "management has elected" to omit such disclosures. May the accountant modify the wording of his report, for example, to state that "Management has not included substantially all of the disclosures . . ." or "The Company has not included substantially all of the disclosures . . ."?

.30 *Interpretation*—Use of the language in the third paragraph of the standard report in paragraph 21 of SSARS 1 [section 100.21] is encouraged; it was designed to impress upon management and the users of financial statements that omission of substantially all disclosures is the entity's decision, not the accountant's. However, provided the report clearly indicates this, the wording "Management has elected to omit" may be modified. Language such as "These financial statements do not include substantially all of the disclosures . . ." should not be used because some might infer that the decision to omit disclosures was the accountant's.

[Issue Date: May, 1982.]

10. Reporting on Tax Returns

.31 *Question*—May an accountant comply with a request from a nonpublic entity to issue a compilation or review report on financial information contained in a tax return, as in Form 1040, *U.S. Individual Income Tax Return,* or Form 1120, *U.S. Corporation Income Tax Return,* or in an information return, as in Form 990, *Return of Organization Exempt from Income Tax,* Form 1065, *U.S. Partnership Return of Income,* or Form 5500, *Return of Employee Benefit Plan?*

.32 *Interpretation*—SSARS 1 [section 100] imposes no requirement on an accountant to report on financial information contained in a tax return. The fact that a return is subsequently used for a purpose other than submission to taxing authorities does not affect that exception. However, an accountant may decide to accept an engagement to issue a compilation or review report on such a return. In that case, he must comply with the applicable performance and reporting standards.

[Issue Date: November, 1982.]

11. Reporting on Uncertainties

.33 *Question*—Paragraph 39 of SSARS 1 [section 100.39] requires an accountant to consider modification of the standard compilation or review report when he becomes aware of a departure from generally accepted accounting principles (which include adequate disclosure) that is material to the financial statements. What guidance should the accountant follow in evaluating the disclosure of an uncertainty?

.34 *Interpretation*—FASB Statement No. 5 [AC section C59], *Accounting for Contingencies,* Statement No. 47 [AC section C32], *Disclosure of Long-Term Obligations,* and other authoritative accounting literature provide guidance on disclosure of uncertainties. However, the accounting literature does not provide specific guidance on disclosure of uncertainties caused by concern about the entity's ability to continue as a going concern. In evaluating the disclosure of those uncertainties, the accountant should look to the guidance provided by paragraphs 10 and 11 of SAS No. 59 [AU section 341.10—.11], *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern.*

.35 If the accountant believes that the disclosure of an uncertainty is inadequate, he should consider the guidance provided in paragraphs 39—41 [section 100.39—.41], and Interpretations 6 and 7 [see JofA, Aug. 81, pp. 111—112], of SSARS 1 [section 9100.18—.26] in modifying his report.

.36 *Question*—If the accountant believes that the financial statements appropriately disclose an uncertainty that is not susceptible of reasonable estimation, is the accountant required to issue a compilation or review report with an explanatory paragraph, describing the matter giving rise to the uncertainty?

.37 *Interpretation*—No. Footnote 18 to paragraph 40 of SSARS 1 [section 100.40, footnote 18] indicates that an accountant is not required to modify his compilation or review report for an uncertainty that is appropriately disclosed in the financial statements.

.38 Although not a requirement, an accountant may wish to draw attention to an uncertainty in an explanatory paragraph of his compilation or review report. If so, the following example may be useful:

"As discussed in Note X, certain conditions indicate that the Company may be unable to continue as a going concern. The accompanying financial statements do not include any adjustments to the financial statements that might be necessary should the Company be unable to continue as a going concern."

.39 *Question*—Paragraph 19 of SSARS 1 [section 100.19] allows the accountant, when he is requested to do so, to compile financial statements that omit substantially all of the disclosures required by GAAP, provided his report clearly indicates the omission and the client's decision to omit the disclosures was not, to the accountant's knowledge, undertaken with the intention of misleading users of the statements. Paragraph 20 [section 100.20] states that disclosure of the use of a comprehensive basis of accounting other than GAAP can never be omitted. Should disclosure of an uncertainty be considered so significant that it also could never be omitted?

.40 *Interpretation*—No. Paragraph 20 of SSARS 1 [section 100.20] requires disclosure of the use of a comprehensive basis of accounting other than

GAAP in an attached footnote, in a note on the face of the financial statements, or in the accountant's report because a user has a right to expect, in the absence of evidence to the contrary, that the financial statements are prepared in conformity with *generally accepted* accounting principles. As to all other matters, the user is adequately warned of the limitations of the financial statements by the report language suggested in paragraph 21 of SSARS 1 [section 100.21] (as amended by SSARS 5).

[Issue Date: December, 1982.]

12. Reporting on a Comprehensive Basis of Accounting Other Than Generally Accepted Accounting Principles

.41 *Question*—Footnote 4 to paragraph 4 of SSARS 1 [section 100.04, footnote 4] states that "reference to generally accepted accounting principles in this statement includes, where applicable, another comprehensive basis of accounting." What modifications to the standard compilation or review report are required when financial statements are prepared on another comprehensive basis of accounting?

.42 *Interpretation*—When financial statements are prepared in accordance with a comprehensive basis of accounting other than generally accepted accounting principles, the footnotes ordinarily would state the basis of presentation and describe how that basis differs from generally accepted accounting principles. If such disclosures are made, the standard forms of compilation and review reports included in SSARS 1 [section 100] (as amended by SSARS 5) should be used. The reports should be modified to appropriately identify the accompanying financial statements.[1]

.43 When an accountant compiles financial statements that are presented in accordance with a comprehensive basis of accounting other than generally accepted accounting principles and that omit substantially all disclosures, paragraph 20 of SSARS 1 [section 100.20] requires disclosure of the basis of accounting. This disclosure may be in an attached footnote or in a note on the face of the financial statements. If disclosure is not made as part of the financial statements, modification of the accountant's compilation report would be required. For example, the following sentence could be added to the first paragraph of the standard compilation report: "The financial statements have been prepared on the accounting basis used by the Company for Federal income tax purposes, which is a comprehensive basis of accounting other than generally accepted accounting principles."

.44 *Question*—Although SSARS 1 [section 100] permits an accountant to compile or review financial statements prepared in conformity with a comprehensive basis of accounting other than generally accepted accounting principles, all the report examples in SSARS are for financial statement presentations in conformity with GAAP. What are appropriate compilation and review reports for other comprehensive bases of accounting?

.45 *Interpretation*—The following examples are offered.

Compilation, Full Disclosure—Cash Basis

I (we) have compiled the accompanying statement of assets and liabilities arising from cash transactions of XYZ Company as of December 31, 19XX, and the related statement of revenue collected and expenses paid for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

---

[1] Refer to paragraph 7 of SAS No. 62 [AU section 623.07].

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Compilation, Omission of Substantially All Disclosures, With No Reference to Basis—Income Tax Basis

I (we) have compiled the accompanying statement of assets, liabilities, and equity-income tax basis of XYZ Company as of December 31, 19XX, and the related statement of revenue and expense-income tax basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. The financial statements have been prepared on the accounting basis used by the Company for Federal income tax purposes, which is a comprehensive basis of accounting other than generally accepted accounting principles.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the disclosures ordinarily included in financial statements prepared on the income tax basis of accounting. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's assets, liabilities, equity, revenue, and expenses. Accordingly, these financial statements are not designed for those who are not informed about such matters.

Review—Income Tax Basis

I (we) have reviewed the accompanying statement of assets, liabilities, and equity-income tax basis of XYZ Company as of December 31, 19XX, and the related statement of revenue and expenses-income tax basis for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the income tax basis of accounting, as described in Note X.

[Issue Date: December, 1982; Revised: November, 1992.]

13. Additional Procedures

.46 *Question*—Certain procedures, such as confirmation of receivables and observation of inventories, are customarily performed in an audit but not in compilation or review engagements. If an accountant performs such "auditing procedures" in connection with a compilation or review engagement, is he required to change the engagement to an audit?

.47 *Interpretation*—No. Paragraph 12 of SSARS 1 [section 100.12] states that in a compilation engagement there is no requirement "to verify, corroborate, or review information," but it does not preclude the accountant from making inquiries or performing additional procedures. Similarly, paragraph 30 of SSARS 1 [section 100.30] states that a review engagement "does not contemplate obtaining an understanding of the internal control structure or assessing control risk, tests of accounting records and of responses to inquiries by obtaining corroborating evidential matter, and certain other procedures ordinarily performed during an audit." However, it also indicates that there may be circumstances when the accountant "should perform the additional procedures he deems necessary. . . ." These citations make it clear that the standards for performing compilations or reviews of financial statements do not preclude the accountant from performing procedures that he deems necessary or that his client requests.

.48 Paragraph 8 of SSARS 1 [section 100.08] does require the accountant to establish an understanding with the entity regarding the services to be performed, including "a description of the report the accountant expects to render," and this understanding establishes the terms and objectives of the engagement. When the accountant, in connection with a compilation or review engagement, plans to perform procedures that are customarily applied during an audit, he may wish to place additional importance on whether his understanding with the client should be in writing.

.49 The wording of confirmation requests or other communications related to additional procedures performed in the course of a compilation or review engagement should not use phrases such as "as part of an *audit* of the financial statements" (emphasis supplied).

[Issue Date: March, 1983.]

[14.] Reporting on Financial Statements When the Scope of the Accountant's Procedures Has Been Restricted

[.50—.53] [Withdrawn April, 1990 by the Accounting and Review Services Committee.]

15. Differentiating a Financial Statement Presentation From a Trial Balance

.54 *Question*—Paragraph 1 of SSARS 1 [section 100.01] states that the accountant should not submit unaudited financial statements of a nonpublic entity to a client or others unless he or she complies with the provisions of SSARS 1. Paragraph 4 of SSARS 1 [section 100.04] defines a financial statement as "a presentation of financial data, including accompanying notes, derived from accounting records and intended to communicate an entity's economic resources or obligations at a point in time, or the changes therein for a period of time, in accordance with generally accepted accounting principles or a comprehensive basis of accounting other than generally accepted accounting principles." [2]

.55 When the accountant is engaged to compile or review financial statements of a nonpublic entity, he or she should report on those statements in accordance with the requirements of SSARS 1 [section 100]. When the accountant has not been engaged to perform services in accordance with SSARS 1 [section 100], he or she should avoid performing accounting services that result in accountant-generated financial presentations that are not easily identifiable as either a financial statement or a trial balance. Paragraph 2 of SSARS 1 [section 100.02] specifies that SSARS do not establish standards for other accounting services such as preparing a trial balance. What attributes should an accountant consider when differentiating a financial statement from a trial balance to determine if SSARS apply to the accounting services performed?

.56 *Interpretation*—The accountant should consider, among other matters, the following attributes when (1) determining whether a financial presentation is a financial statement or a trial balance and (2) modifying the presentation to eliminate features in the presentation that blur the distinction between a financial statement and a trial balance.

- Generally, a financial statement features the combination of similar general ledger accounts to create classifications or account groupings with corresponding subtotals and totals of dollar amounts. Some examples of these classifications or account groupings are "current assets," "long-term debt," and "revenues." In addition, contra accounts are generally netted against the related primary accounts in financial statement presentations (i.e., "Accounts Receivable Net of Allowance for Bad Debts"). In contrast, a trial balance consists of a listing of all of the general ledger accounts and their corresponding debit or credit balances.
- Financial statements generally contain titles that identify the presentation as one intended to present financial position, results of operations, or cash flows. Typical titles for financial statements include:
  (a) Balance Sheet
  (b) Statement of Income or Statement of Operations
  (c) Statement of Retained Earnings
  (d) Statement of Cash Flows
  (e) Statement of Changes in Owners' Equity
  (f) Statement of Assets and Liabilities (with or without owners' equity accounts)
  (g) Statement of Revenue and Expenses
  (h) Summary of Operations
  (i) Statement of Operations by Product Lines
  (j) Statement of Cash Receipts and Disbursements

[2] A financial statement may be, for example, that of a corporation, a consolidated group of corporations, a combined group of affiliated entities, a not-for-profit organization, a government unit, an estate or trust, a partnership, a proprietorship, a segment of any of these, or an individual. The method of preparation (for example, manual or computer preparation) is not relevant to the definition of a financial statement. References in this interpretation to generally accepted accounting principles are intended to include a comprehensive basis of accounting other than generally accepted accounting principles.

Examples of typical titles for trial balance presentations are:

(a) Trial Balance

(b) Working Trial Balance

(c) Adjusted Trial Balance

(d) Listing of General Ledger Accounts

- The balance sheet in a set of financial statements segregates asset, liability, and owners' equity accounts and presents these three elements based on the following basic example equation:

$$\text{Assets} = \text{Liabilities} + \text{Owners' Equity}$$

The elements of the income statement and their relationship to net income are presented based on the following basic example equation:

$$\text{Revenues} - \text{Expenses} + \text{Gains} - \text{Losses} = \text{Net Income}$$

In a trial balance, no attempt is made to establish a mathematical relationship among the elements except that total debits equal total credits.

- The income statement in a set of financial statements generally contains a caption such as "Net Income" or "Net Revenues over Expenses" that identifies the net results of operations. Trial balance presentations generally do not contain similar captions.
- The balance sheet in a set of financial statements usually presents assets in the order of their liquidity and liabilities in the order of their maturity. In a trial balance, the accounts are generally listed in account number order as they appear in the general ledger.
- In a set of financial statements, the income statement articulates with the balance sheet because the net results of operations are added to or subtracted from opening retained earnings. In a trial balance, the net results of operations are generally not closed out to retained earnings.

.57 The accountant should use judgment when considering these attributes to determine whether the financial presentation constitutes a financial statement or a trial balance. When making this determination, the accountant should consider the preponderance of the attributes of the financial presentation. For example, a trial balance that contains one or two attributes of a financial statement may, in the accountant's judgment, still constitute a trial balance. When the presentation is deemed to be a financial statement and the accountant does not modify the presentation to conform with the attributes of a trial balance, the accountant, at a minimum, should compile the financial statements in accordance with SSARS 1 [section 100].

[Issue Date: September, 1990.]

[16.] Determining if the Accountant has "Submitted" Financial Statements Even When Not Engaged to Compile or Review Financial Statements

[.58-.60] [Withdrawn by the issuance of Statement on Standards for Accounting and Review Services 7, November 1992.] [3]

[3] Footnote deleted by the issuance of Statement on Standards for Accounting and Review Services 7, November 1992.

17. Submitting Draft Financial Statements

.61 *Question*—Accountants frequently submit draft financial statements (1) because information needed to complete a compilation or review of the financial statements will not be available until a later date or (2) to provide the client with the opportunity to read and analyze the financial statements prior to their final issuance. Is it permissible for the accountant to submit draft financial statements without intending to comply with the reporting provisions of SSARS 1 [section 100]?

.62 *Interpretation*—No. An accountant should not submit draft financial statements without intending to submit those financial statements in final form accompanied by an appropriate compilation or review report prescribed by SSARS 1 [section 100]. However, as long as the accountant intends to submit the financial statements in final form and labels each page of draft financial statements with words such as "Draft," "Preliminary Draft," "Draft—Subject to Changes," or "Working Draft," the accountant is not required to comply with the reporting provisions of SSARS 1 [section 100] with respect to those draft financial statements. In the rare circumstance where the accountant intended to but never submitted final financial statements, the accountant may want to document the reasons why he or she was unable to submit those financial statements.

[Issue Date: September, 1990.]

18. Special-Purpose Financial Presentations to Comply With Contractual Agreements or Regulatory Provisions

.63 *Question*—An accountant may be asked to report on special-purpose financial statements prepared to comply with a contractual agreement [4] or regulatory provision that specifies a special basis of presentation. [5] In those circumstances, can the accountant issue a compilation or review report on those financial statements in accordance with SSARS 1 [section 100], *Compilation and Review of Financial Statements?*

.64 *Interpretation*—Yes. An accountant who is asked to report on special-purpose financial statements prepared to comply with a contractual agreement or regulatory provision that specifies a special basis of presentation may issue a compilation or review report on those financial statements in accordance with SSARS 1 [section 100] as described in this interpretation. This interpretation describes reporting on presentations based on contractual agreements or regulatory provisions that require a financial presentation that

a) does not constitute a complete presentation of the entity's assets, liabilities, revenues, or expenses, but is otherwise prepared in conformity with generally accepted accounting principles (GAAP) or an other comprehensive basis of accounting (OCBOA) [6]

or

b) is a prescribed basis of accounting that does not result in a presentation in conformity with GAAP or OCBOA.

Incomplete Presentation That Is Otherwise in Conformity With GAAP or an OCBOA

.65 An entity may engage an accountant to compile or review a special-purpose financial presentation prepared in compliance with a contractual agreement or regulatory provision that does not constitute a complete presentation of the entity's assets, liabilities, revenues or expenses, but is otherwise prepared in conformity with GAAP or OCBOA. For example, a purchase agreement may require an entity to provide a schedule of net assets sold, measured in conformity with GAAP, but limited to the asset to be sold and liabilities to be transferred. Also, a governmental agency may require a schedule of revenues and certain expenses for an entity in which revenues and expenses are measured in conformity with GAAP, but expenses are defined to exclude certain items such as interest, depreciation, and income taxes. These special-purpose financial presentations should generally be considered as financial statements even though certain items may be excluded. Therefore, in such cases, the presentations would not be considered as presentations of a specified element, account, or item of a financial statement as discussed in paragraphs .27 through .28.

.66 Compiled or reviewed special-purpose financial statements prepared in accordance with a contractual agreement or regulatory provision that do not constitute a complete presentation of the entity's assets, liabilities, reve-

---

[4] A contractual agreement as discussed in this interpretation is an agreement between the client and one or more third parties other than the accountant.

[5] When the contractual agreement or regulatory provision specifies the use of a prescribed form for which the accountant has been engaged to compile the financial statements included therein, the accountant should reference SSARS 3 [section 300], *Compilation Reports on Financial Statements Included in Certain Prescribed Forms,* for an alternative form of standard compilation report when the prescribed form calls for a departure from generally accepted accounting principles or another comprehensive basis of accounting.

[6] The term "comprehensive basis of accounting other than generally accepted accounting principles" is defined in SAS No. 62, *Special Reports,* paragraph 4 [AU section 623.04].

nues or expenses, but are otherwise prepared in conformity with GAAP or OCBOA, should:

a) Include the disclosure of the basis of presentation in the notes to the financial statements.

b) Differ from financial statements prepared in accordance with GAAP or OCBOA only to the extent necessary to meet the special purpose for which the presentation is prepared.

c) Contain similar informative disclosures when the presentation contains items that are the same as, or similar to, those contained in a full set of financial statements.

d) Include titles that avoid any implication that the special-purpose financial statements are intended to present financial position, results of operations, or cash flows.

.67 When reporting on compiled or reviewed special-purpose financial statements prepared in accordance with a contractual agreement or regulatory provision that does not constitute a complete presentation of the entity's assets, liabilities, revenues or expenses, but is otherwise prepared in conformity with GAAP or OCBOA, the accountant's report should be expanded to include two explanatory paragraphs with the following information. A(n):

First Additional Paragraph

- Explanation of what the presentation is intended to present and reference to a note to the financial statements that describes the basis of accounting. In a compilation engagement in which the entity chooses to omit substantially all of the disclosures and does not disclose in the financial statements the basis of presentation, the accountant should disclose the basis in the compilation report.
- Indication that the presentation is not intended to be a complete presentation of the entity's assets, liabilities, revenues, and expenses.[7]

Second Additional Paragraph

- Statement that the distribution of the report is restricted to those within the entity, to parties to the contract or agreement, for filing with a regulatory agency, or to those with whom the entity is negotiating directly. (Certain reports filed with regulatory agencies are a matter of public record. In those circumstances, the report should state that the restriction is not intended to limit the distribution of the report, which is a matter of public record.)

Compilation of Special-Purpose Financial Presentation That is an Incomplete Presentation Prepared in Accordance With a Contractual Agreement but is Otherwise in Conformity With GAAP or OCBOA

(Note: The two paragraphs to be added to the standard compilation report are italicized.)

I (We) have compiled the accompanying statement of net assets sold of XYZ Company as of December 31, 19XX, in accordance with

[7] If the basis of presentation is OCBOA, the paragraph should state that the basis of presentation is a comprehensive basis of accounting other than generally accepted accounting principles and that it is not intended to be a complete presentation of the entity's assets, liabilities, revenues, and expenses on the basis described.

Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying statement and, accordingly do not express an opinion or any form of assurance on it.

The accompanying statement was prepared to present the net assets of XYZ Company sold to ABC Company pursuant to the purchase agreement described in Note A, and is not intended to be a complete presentation of XYZ Company's assets and liabilities.

This report is intended solely for the information and use of the boards of directors and managements of XYZ Company and ABC Company and should not be used for any other purpose.

Review of Special-Purpose Financial Presentation That is an Incomplete Presentation Prepared in Accordance With a Regulatory Provision but is Otherwise in Conformity With GAAP or OCBOA

(Note: The two paragraphs to be added to the standard review report are italicized. Also, because the report in this example will be filed with a regulatory agency and made available as a part of the public record, the report restriction is modified accordingly.)

I (We) have reviewed the accompanying statement of gross income and direct operating expenses of XYZ Company as of December 31, 19XX, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in this statement is the representation of management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the statement taken as a whole. Accordingly, I (We) do not express such an opinion.

The accompanying statement was prepared to present gross income and direct operating expenses of XYZ Company pursuant to the regulatory provision described in Note A, and is not intended to be a complete presentation of XYZ Company's gross income and expenses.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying statement of gross income and direct operating expenses in order for it to be in conformity with generally accepted accounting principles.

This report is intended for the information and use of the board of directors and management of XYZ Company and [specify legislative or regulatory agency]. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Presentation Prescribed in a Contractual Agreement That is Not in Conformity With GAAP or an OCBOA

.68 An entity may engage an accountant to compile or review a special-purpose financial presentation prepared in conformity with a basis of accounting prescribed in a contractual agreement that results in a presentation that is not in conformity with GAAP or OCBOA. For example, an acquisition agreement may require an entity to prepare financial statements in which certain assets, such as inventories and properties, are presented in conformity with a valuation basis, that is neither GAAP or OCBOA. Also, a loan agreement may require the borrower to prepare financial statements in which certain assets, such as receivables, inventories, and properties are presented on a basis specified in the agreement that is neither GAAP or OCBOA. In these circumstances, the special-purpose financial presentations are not considered to be prepared in conformity with an OCBOA because the criteria used to prepare such financial statements do not meet the requirement of being "criteria having substantial support," even though the criteria are definite.

.69 Compiled or reviewed special-purpose financial statements prepared in conformity with a contractual agreement that is not in conformity with GAAP or OCBOA should:

(a) Include the disclosure of the basis of presentation in the notes to the financial statements.

(b) Contain similar informative disclosures when the presentation contains items that are the same as, or similar to, those contained in GAAP or OCBOA financial statements.

(c) Include titles that avoid any implication that the special-purpose financial statements are intended to present financial position, results of operations, or cash flows.

.70 When reporting on compiled or reviewed special-purpose financial statements prepared in accordance with a contractual agreement that does not conform to GAAP or OCBOA, the accountant's report should be expanded to include two explanatory paragraphs with the following information. A(n):

First Additional Paragraph

- Explanation of what the presentation is intended to present, reference to a note to the financial statements that describes the basis of presentation, and explanation that the presentation is not intended to be a presentation in conformity with generally accepted accounting principles. In a compilation engagement in which the entity chooses to omit substantially all of the disclosures and does not disclose in the financial statements the basis of presentation, the accountant should disclose the basis in the compilation report.
- Description of any significant interpretations made by management of the contractual agreement.

Second Additional Paragraph

- Statement that the distribution of the report is restricted to those within the entity, to parties to the contract or agreement, or to those with whom the entity is negotiating directly.

.71 The accountant's standard review report includes a statement that he or she is not aware of any material modifications that should be made to the financial statements in order for them to be "in conformity with GAAP." However, when the accountant is engaged to report on a special-purpose financial presentation pursuant to a contractual agreement that results in a presentation that does not conform with GAAP or OCBOA, the accountant should modify the report to reference the basis of accounting prescribed by the contractual agreement referred to in the notes since the presentation is not intended to conform with GAAP.

.72 If the accountant becomes aware that the information the presentation is intended to present contains a departure from the basis of presentation described that is material to the financial statements, the accountant should consider whether modification of his or her report is adequate to disclose such departure. In those circumstances, the accountant should consider the guidance in paragraphs 39 through 41 of SSARS 1 [section 100.39-.41].

Compilation of Special-Purpose Financial Presentation Pursuant to an Acquisition Agreement That Results in a Presentation That is Not in Conformity With GAAP or OCBOA

(Note: The two paragraphs to be added to the standard compilation report are italicized.)

I (We) have compiled the special-purpose statement of assets and liabilities of XYZ Company as of December 31, 19XX and the related special-purpose statements of revenues and expenses and of cash flows for the year then ended in accordance with standards established by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying special-purpose financial statements and, accordingly, do not express an opinion or any form of assurance on them.

The accompanying special-purpose financial statements were prepared for the purpose of complying with the acquisition agreement between ABC Company and XYZ Company described in Note A, and are not intended to be a presentation in conformity with generally accepted accounting principles.

This report is intended for the information and use of the boards of directors and managements of XYZ Company and ABC Company and should not be used for any other purpose.

Review of Special-Purpose Financial Presentation Pursuant to a Contractual Agreement That Results in a Presentation That is Not in Conformity With GAAP or OCBOA

(Note: The two paragraphs to be added to the standard review report are italicized.)

I (We) have reviewed the accompanying special-purpose statement of assets and liabilities of XYZ Company as of December 31, 19XX and the related special-purpose statements of revenues and expenses and of cash flows for the year then ended in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (We) do not express such an opinion.

The accompanying special-purpose financial statements were prepared for the purpose of complying with Section 4 of a loan agreement between DEF Bank and XYZ Company as discussed in Note A, and *are not intended to be a presentation in conformity with generally accepted accounting principles.*

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying special-purpose financial statements in order for them to be in conformity with the basis of accounting described in Note A.

This report is intended solely for the information and use of the boards of directors and managements of XYZ Company and DEF Bank and should not be used for any other purpose.

[Issue Date: September, 1990.]

19. Reporting When Financial Statements Contain a Departure From Promulgated Accounting Principles That Prevents the Financial Statements From Being Misleading

.73 *Question*—Rule 203 [ET section 203.01] of the AICPA Code of Professional Conduct states:

> A member shall not (1) express an opinion or state affirmatively that the financial statements or other financial data of any entity are presented in conformity with generally accepted accounting principles or (2) state that he or she is not aware of any material modifications that should be made to such statements or data in order for them to be in conformity with generally accepted accounting principles, if such statements or data contain any departure from an accounting principle promulgated by bodies designated by Council to establish such principles that has a material effect on the statements or data taken as a whole. If, however, the statements or data contain such a departure and the member can demonstrate that due to unusual circumstances the financial statements or data would otherwise have been misleading, the member can comply with the rule by describing the departure, its approximate effects, if practicable, and the reasons why compliance with the principle would result in a misleading statement.

Paragraphs 39 through 41 of SSARS 1 [section 100.39—.41] do not address the Rule 203 [ET section 203.01] circumstances. When the circumstances contemplated by Rule 203 [ET section 203.01] are present, how should the accountant report on the information described in the rule?

.74 *Interpretation*—When the circumstances contemplated by Rule 203 [ET section 203.01] are present in a review engagement, the accountant's review report should include, in a separate paragraph or paragraphs, the information required by Rule 203 [ET section 203.01]. In such a case, the accountant would not modify the standard review report, except for the addition of the separate paragraph(s) that contains the information required by Rule 203 [ET section 203.01], unless there are other reasons to do so that are not associated with the departure from a promulgated principle.

.75 Rule 203 [ET section 203.01] does not apply to compilation engagements. Accordingly, when the accountant is performing a compilation engagement and is confronted with the circumstances contemplated by Rule 203 [ET section 203.01], the guidance in paragraphs 39 through 41 of SSARS 1 [section 100.39—.41] pertaining to departures from generally accepted accounting principles should be followed.

[Issue Date: February, 1991.]

20. Applicability of Statements on Standards for Accounting and Review Services to Litigation Services

.76 *Question*—Statements on Standards for Accounting and Review Services (SSARS) do not apply to the types of accounting services exemplified in paragraph 2 of SSARS 1, *Compilation and Review of Financial Statements* [section 100.02]. When are litigation services excluded from the applicability of SSARS?

.77 *Interpretation*—SSARS do not apply to financial statements submitted in conjunction with litigation services that involve pending or potential formal legal or regulatory proceedings before a "trier of fact" [8] in connection with the resolution of a dispute between two or more parties when the:

(a) Service consists of being an expert witness.

(b) Service consists of being a "trier of fact" or acting on behalf of one.

(c) Accountant's work under the rules of the proceedings is subject to detailed analysis and challenge by each party to the dispute.

(d) Accountant is engaged by an attorney to do work that will be protected by the attorney's work product privilege and such work is not intended to be used for other purposes.

When performing such litigation services the accountant should comply with Rule 201, *General Standards* [ET section 201.01], of the AICPA Code of Professional Conduct.

.78 *Question*—When do SSARS apply to litigation service engagements?

.79 *Interpretation*—SSARS apply to litigation service engagements when the accountant:

(a) Submits unaudited financial statements of a nonpublic entity that are the representation of management (owners) to others who under the rules of the proceedings do not have the opportunity to analyze and challenge the accountant's work, or

(b) Is specifically engaged to submit, in accordance with SSARS, financial statements that are the representation of management (owners).

[Issue Date: May, 1991.]

---

[8] A "trier of fact" in this section means a court, regulatory body, or government authority; their agents; a grand jury; or an arbitrator or mediator of the dispute.

AR Section 9200

Reporting on Comparative Financial Statements: Accounting and Review Services Interpretations of Section 200

1. Reporting on Financial Statements that Previously Did Not Omit Substantially All Disclosures

.01 *Question*—Paragraph 29 of SSARS 2 [section 200.29], *Reporting on Comparative Financial Statements,* states that an accountant who has compiled, reviewed, or audited financial statements that do not omit substantially all of the disclosures required by generally accepted accounting principles may subsequently compile financial statements for the same period that do omit substantially all of those disclosures when they are to be presented in comparative financial statements. In these circumstances, SSARS 2 [section 200] requires the accountant's compilation report to include an additional paragraph indicating (a) the nature of the service rendered with respect to the financial statements that previously did not omit substantially all disclosures and (b) the date of his previous report.

.02 When the accountant has previously audited such financial statements, he may have issued a qualified opinion (see paragraphs 38—39 of SAS No. 58 [AU section 508.38—.39], *Reports on Audited Financial Statements*) or an adverse opinion (see paragraphs 67—69 of SAS No. 58) [AU section 508.67—.69], or he may have disclaimed an opinion (see paragraphs 70—72 of SAS No. 58 [AU section 508.70—.72]). What effect, if any, should this have on the accountant's report on the comparative compiled financial statements? Also, when the accountant has previously compiled or reviewed such financial statements, what effect should a modification to his compilation or review report (see paragraphs 39 to 41 of SSARS No. 1 [section 100.39—.41]) have on the accountant's report on the comparative compiled financial statements?

.03 *Interpretation*—If financial statements that omit substantially all disclosures are compiled from financial statements that the accountant has previously audited, his report on the comparative compiled financial statements should indicate whether he expressed a qualified or adverse opinion, or disclaimed an opinion, on the audited financial statements, and the substantive reasons therefor. Similarly, if the accountant issued a modified compilation or review report or a report containing any paragraphs emphasizing a matter regarding the financial statements (see paragraphs 39 to 41 of SSARS No. 1 [section 100.39—.41]) on financial statements that previously did not omit substantially all disclosures, the accountant's reference to that report in his report on the comparative compiled financial statements should include a description or a quotation of any modifications of the standard report and of any paragraphs emphasizing a matter regarding the financial statements.

.04 Statements on standards for accounting and review services do not require an accountant to modify the standard compilation or review report for an uncertainty or an inconsistency in the application of generally accepted accounting principles. When the accountant's report on comparative compiled financial statements that omit substantially all of the disclosures required by generally accepted accounting principles includes a reference to a previous audit report that includes an explanatory paragraph describing an uncertainty, users may assume, in the absence of an indication to the contrary, that the uncertainty has been resolved. Thus, in such circumstances, the accountant should consider the desirability of emphasizing the uncertainty in a separate paragraph of that portion of his report that relates to the financial statements for the current period.

[Issue Date: November, 1980.]

AR Section 9300

Compilation Reports on Financial Statements Included in Certain Prescribed Forms: Accounting and Review Services Interpretations of Section 300

1. Omission of Disclosures in Financial Statements Included in Certain Prescribed Forms

.01 *Question*—The accountant may have reviewed financial statements including disclosures required by generally accepted accounting principles and be asked to compile financial statements included in a prescribed form which does not request such disclosures. If the measurement principles to be used do not cause the compiled financial statements in the prescribed form to be materially different from the reviewed statements, can the accountant's compilation report on the prescribed form refer to the accountant's report on the reviewed financial statements?

.02 *Interpretation*—Yes. The footnote to paragraph 5 of SSARS 1 [section 100.05] (as amended) permits an accountant who has reviewed the financial statements of a nonpublic entity to issue a compilation report on financial statements for the same period that are included in a prescribed form that calls for a departure from generally accepted accounting principles. When the difference between the previously reviewed financial statements and the financial statements included in the prescribed form is limited to the omission of disclosures not requested by the form, the accountant may wish to refer to his review report in his report on the compiled financial statements included in the prescribed form. This might be accomplished by adding a sentence such as the following to the second paragraph of the report illustrated in paragraph 3 of SSARS 3 [section 300.03] or as a separate paragraph: "These financial statements were compiled by me (us) from financial statements for the same period which I (we) previously reviewed, as indicated in my (our) report dated ______________."* The reference to a previous review report should include a description or a quotation of any modifications of the standard review report previously issued and of any paragraphs emphasizing a matter regarding the financial statements.

.03 If the measurement principles used in the compiled financial statements in the prescribed form cause such financial statements to be materially different from the previously reviewed financial statements, no reference should be made to the review engagement.

[Issue Date: May, 1982]

---

* The report included in paragraph 3 of SSARS 3 [section 300.03] is an alternate form of report. If the accountant elects to use the standard compilation report included in SSARS 1, paragraph 17 [section 100.17] this sentence may be added to that report.

AR Section 9400

Communications Between Predecessor and Successor Accountants: Accounting and Review Services Interpretations of Section 400

1. Reports on the Application of Accounting Principles

.01 *Question*—SSARS 4, *Communications Between Predecessor and Successor Accountants* [section 400], provides guidance on communication between a successor accountant who has been invited to propose on a compilation or review engagement or who has accepted such an engagement and a predecessor accountant who has resigned or who has been notified that his services have been terminated. The guidance provided concerns only the situation in which one accountant succeeds another in a compilation or review engagement.

.02 In other situations, an accountant in public practice may be requested by an entity that has not engaged that accountant to report on its financial statements to provide advice about the application of accounting principles or about the type of report to be issued on its financial statements (compilation, review, or audit report). Such requests are often made to obtain a second opinion about these matters from another accountant. What guidance should be followed by the accountant who is requested to provide advice on these matters?

.03 *Interpretation*—SAS No. 50, *Reports on the Application of Accounting Principles* [AU section 625], applies to any accountant in public practice asked to provide written advice on the application of accounting principles to specified transactions (either completed or proposed), on the type of report that may be rendered on a specific entity's financial statements, or to intermediaries on the application of accounting principles not involving facts or circumstances of a particular principal.

.04 SAS No. 50 also applies to oral advice on the application of accounting principles to a specific transaction, or the type of report that may be rendered on any entity's financial statements, when the reporting accountant concludes the advice is intended to be used by a principal to the transaction as an important factor considered in reaching a decision.

.05 Paragraph 7 of SAS No. 50 states that the reporting accountant who is requested to provide such written or oral advice by an entity should consult with that entity's accountant, if any, to ascertain all the available facts relevant to forming a professional judgment. The reporting accountant should follow the performance and reporting guidance in SAS No. 50 for such engagements.

[Issue Date: August, 1987.]

AR Section 9600

Reporting on Personal Financial Statements Included in Written Personal Financial Plans: Accounting and Review Services Interpretation of Section 600

1. Submitting a Personal Financial Plan to a Client's Advisers

.01 *Question*—Paragraph 3 of Statements on Standards for Accounting and Review Services (SSARS) 6, *Reporting on Personal Financial Statements Included in Written Personal Financial Plans* [section 600.03], states that an accountant may submit a written personal financial plan containing unaudited personal financial statements to a client without complying with the requirements of SSARS 1, *Compilation and Review of Financial Statements* [section 100] when, among other conditions, the accountant establishes an understanding with the client that the financial statements will be used solely to assist the client and the client's advisers to develop the client's personal financial goals and objectives. Does developing the client's personal financial goals and objectives encompass implementing the personal financial plan by the client or the client's advisers?

.02 *Interpretation*—Yes. Developing a client's personal financial goals and objectives includes implementing the personal financial plan by the client or the client's advisers because implementing the plan may be considered the culmination of the process of developing personal financial goals and objectives. Therefore, an accountant may submit a written personal financial plan containing unaudited personal financial statements to a client, to be used by the client or the client's advisers to implement the personal financial plan, without complying with the requirements of SSARS 1 [section 100], provided the conditions in paragraph 3 of SSARS 6 [section 600.03] exist.

.03 Examples of implementation of a personal financial plan by the client's advisers include use of the plan by:

- an insurance broker who will identify specific insurance products.
- an investment adviser who will provide specific recommendations about the investment portfolio.
- an attorney who will draft a will or trust documents.

[Issue Date: May, 1991.]

AR Appendix A

Cross-Reference Table for Accounting and Review Services Interpretations

(Sections of the text are cross-referenced to Interpretations)

Section	*Interpretation Subject (Interpretation No.)*	*Interpretation Section*
100	Omission of Disclosures in Reviewed Financial Statements (No. 1)	9100.01-.02
100	Financial Statements Included in SEC Filings (No.2)	9100.03-.05
100	Reporting on the Highest Level of Service (No. 3)	9100.06-.12
100	Planning and Supervision (No. 5)	9100.16-.17
100	Reports on Specified Elements, Accounts, or Items of a Financial Statement (No. 8)	9100.27-.28
100	Reporting on Tax Returns (No. 10)	9100.31-.32
100	Reporting on a Comprehensive Basis of Accounting Other Than Generally Accepted Accounting Principles (No. 12)	9100.41-.45
100	Differentiating a Financial Statement Presentation From a Trial Balance (No. 15)	9100.54-.57
100	Submitting Draft Financial Statements (No. 17)	9100.61-.62
100	Special-Purpose Financial Presentations to Comply With Contractual Agreements or Regulatory Provisions (No. 18)	9100.63-.72
100	Submitting a Personal Financial Plan to a Client's Advisers (No. 1)	9600.01-.03
100.01	Differentiating a Financial Statement Presentation From a Trial Balance (No. 15)	9100.54-.57
100.02	Differentiating a Financial Statement Presentation From a Trial Balance (No. 15)	9100.54-.57
100.02	Applicability of Statements on Standards for Accounting and Review Services to Litigation Services (No. 20)	9100.76-.79
100.04	Financial Statements Included in SEC Filings (No. 2)	9100.03-.05
100.04	Reporting on the Highest Level of Service (No. 3)	9100.06-.12
100.04	Reporting on a Comprehensive Basis of Accounting Other than Generally Accepted Accounting Principles (No. 12)	9100.41-.45
100.04	Differentiating a Financial Statement Presentation From a Trial Balance (No. 15)	9100.54-.57
100.05	Report on the Highest Level of Service (No. 3)	9100.06-.12

Section	*Interpretation Subject (Interpretation No.)*	*Interpretation Section*
100.40	Special-Purpose Financial Presentations to Comply With Contractual Agreements or Regulatory Provisions (No. 18)	9100.63-.72
100.40	Reporting When Financial Statements Contain a Departure From Promulgated Accounting Principles That Prevents the Financial Statements From Being Misleading (No. 19)	9100.73-.75
100.41	Withdrawal from Compilation or Review Engagements (No. 6)	9100.18-.22
100.41	Reporting on Uncertainties (No. 11)	9100.33-.40
100.41	Reporting on Financial Statements that Previously Did Not Omit Substantially All Disclosures (No. 1)	9200.01-.04
100.41	Special-Purpose Financial Presentations to Comply With Contractual Agreements or Regulatory Provisions (No. 18)	9100.63-.72
100.41	Reporting When Financial Statements Contain a Departure From Promulgated Accounting Principles That Prevents the Financial Statements From Being Misleading (No. 19)	9100.73-.75
100.42	Discovery of Information After the Date of the Accountant's Report (No. 4)	9100.13-.15
100.43	Reports on Specified Elements, Accounts, or Items of a Financial Statement (No. 8)	9100.27-.28
200	Reporting on Financial Statements that Previously Did Not Omit Substantially All Disclosures (No. 1)	9200.01-.04
200.01	Financial Statements Included in SEC Filings (No. 2)	9100.03-.05
200.29	Reporting on Financial Statements that Previously Did Not Omit Substantially All Disclosures (No. 1)	9200.01-.04
300	Special-Purpose Financial Presentations to Comply With Contractual Agreements or Regulatory Provisions (No. 18)	9100.63-.72
300.03	Omission of Disclosures in Financial Statements Included in Certain Prescribed Forms (No. 1)	9300.01-.03
400	Reports on the Application of Accounting Principles (No. 1)	9400.01-.05
600.03	Submitting a Personal Financial Plan to a Client's Advisers (No. 1)	9600.01-.03

APPENDIX B

Qs and As — Technical Practice Aids

The inquiries and nonauthoritative replies in this Appendix are from the AICPA *Technical Practice Aids* (TPA), and are based on selected practice problems answered by the staff of the AICPA Technical Information Division. The TPAs have not been approved, disapproved, or otherwise acted upon by the senior technical committees of the AICPA or the FASB.

Table of Contents

Table of Contents (Continued)

Table of Contents (Continued)

APPENDIX B

Qs AND As — TECHNICAL PRACTICE AIDS

B.001 Omission of Reconciliation of Net Income to Cash Flows From Operations

Inquiry — When an accountant is requested to compile financial statements that omit substantially all of the disclosures required by GAAP [SSARS 1, *Compilation and Review of Financial Statements,* paragraph 19], would the omission of the schedule, "reconciliation of net income to net cash flows from operating activities" required by the direct method of reporting cash flows under FASB Statement No. 95, *Statement of Cash Flows,* be considered a departure from GAAP?

Reply — Yes. Under the direct method of reporting net cash flows from operating activities, the separate schedule reconciling net income to net cash flow from operating activities is a required part of the cash flow statement. If the schedule is omitted, the accountant should modify his compilation report to disclose a departure form GAAP in accordance with SSARS 1, paragraph 40. (TPA 1300.17)

B.002 Communications Between Predecessor Accountant and Successor Auditor

Inquiry — An accountant is engaged to audit the current year's financial statements of a company. In the prior year, the company's financial statements were reviewed by another accountant. Is the successor auditor required to communicate with the predecessor accountant?

Reply — Yes. The fact that the prior year's financial statements were reviewed does not relieve the successor auditor of responsibility for communicating with the predecessor accountant.

SAS No. 7, *Communications Between Predecessor and Successor Auditors,* applies whenever an accountant has been retained, or is to be retained, to conduct an audit of financial statements in accordance with generally accepted auditing standards. According to SAS No. 7, paragraph 4, "Inquiry of the predecessor auditor is a necessary procedure because the predecessor may be able to provide the successor with information that will assist him in determining whether to accept the engagement." (TPA 8900.05)

B.003 Change From Generally Accepted Accounting Principles (GAAP) to An Other Comprehensive Basis of Accounting (OCBOA) or From OCBOA to GAAP

Inquiry — A company that has previously issued financial statements prepared in accordance with GAAP has decided to change to the income tax basis (or vice versa). How should the change in accounting basis be accounted for and reported in the financial statements and how does the change impact the auditor's or accountant's report?

Reply —
Accounting issues:

Authoritative literature does not address accounting for a change in accounting basis. APB Opinion No. 20, *Accounting Changes* (AC A06), provides guidance for reporting accounting changes within the same basis. However, the situation described above is considered to be a change in accounting basis rather than an accounting change.

When only current year financial statements are presented, it is common practice to present the effect of the change in the accounting basis by showing beginning retained earnings as previously reported with an adjustment to convert to the new basis. Although not as common in practice, precedent also exists for either showing opening retained earnings on the new basis or showing the effects of the change as a cumulative-effect adjustment in the income statement.

However, if comparative financial statements are presented, the prior year(s) should be restated and presented under the basis to which the company has changed. Restatement is necessary to ensure comparability with all periods presented.

In both cases, the change in accounting basis should be disclosed in the notes to the financial statements.

Reporting issues:

Auditing literature states that a change in accounting basis does not represent a lack of consistency and, consequently, that report modification is not required. However, the literature allows for the inclusion of an explanatory paragraph in the auditor's report to emphasize a matter regarding the financial statements.

A summary of the relevant authoritative references follows:

SAS No. 58, *Reports on Audited Financial Statements*, paragraph 34 (AU section 508.34) — *Lack of Consistency*, indicates that the consistency reference in the auditor's report refers to consistent application of principles within a basis of presentation. The standards do not address the consistent use of a basis of presentation; therefore, a change in accounting basis does not require the auditor to modify the report for a lack of consistency.

Also, SAS No. 62, *Special Reports*, footnote 33 (AU section 623.31, footnote 33) — Circumstances Requiring Explanatory Language in an Auditor's Special Report, indicates that a change from GAAP to an OCBOA does not represent a lack of consistency in accounting principles and states, in part, that an auditor may wish to add an explanatory paragraph to highlight a difference in the basis of presentation in the current year from that used in the prior year. Footnote 33 (AU section 623.31, footnote 33) does not address changes from an OCBOA to GAAP or whether an explanatory paragraph is suggested for both single-period and comparative statements. However, the auditor may consider adding an explanatory paragraph in each of these situations.

SAS No. 58, paragraph 37 (AU section 508.37), indicates that an auditor reporting on GAAP financial statements may wish to emphasize an accounting matter affecting the comparability of financial statements with those of the preceding period. SAS No. 62, paragraph 31 (AU section 623.31), provides that an auditor reporting on OCBOA statements may wish to modify the report to emphasize a matter similar to reporting on GAAP statements.

A sample explanatory paragraph for an audit report on comparative financial statements in the year of change to an OCBOA follows:

(explanatory paragraph)

> As discussed in Note A to the financial statements, in 19X4 the Company adopted a policy of preparing its financial statements on the accrual method of accounting used for federal income tax purposes, which is a comprehensive basis of accounting other than generally accepted accounting principles. Accordingly, the accompanying financial statements are not intended to present financial position and results of operations in conformity with generally accepted accounting principles. The financial statements for 19X3 have been restated to reflect the income tax basis of accounting (accrual method) adopted in 19X4.

Accountants performing review or compilation engagements may also consider adding an explanatory paragraph for these basis changes. [Amended February 1995.](TPA 9210.10)

B.004 Compilation of Supplementary Schedules in Audited Financial Statements

Inquiry — When supplementary schedules are included with audited financial statements in an auditor-submitted document, can these schedules be compiled in accordance with SSARS 1, *Compilation and Review of Financial Statements,* paragraph 43?

Reply — No. It would not be appropriate to refer to the accounting and review services literature to report on the accompanying information in this situation. If such schedules accompany financial statements audited in accordance with generally accepted auditing standards, the guidance in SAS No. 29, *Reporting on Information Accompanying the Basic Financial Statements in Auditor-Submitted Documents,* should be followed. SAS No. 29, paragraph 6d, states that the auditor should either express or disclaim an opinion on the information, depending on whether it has been subjected to the auditing procedures applied in the audit of the basic financial statements. (TPA 9410.14)

B.005 Statement of Cash Receipts and Disbursements

Inquiry — What is the appropriate language for audit, review, and compilation reports on a statement of cash receipts and disbursements?

Reply — Report language will vary depending on the level of service performed. A statement of cash receipts and disbursements is a financial statement prepared under an other comprehensive basis of accounting (see SAS No. 62, *Special Reports* (AU 623.04), and SSARS 1, *Compilation and Review of Financial Statements* (AR 100.04)). It is a pure cash-basis financial statement that summarizes cash activity of the entity, including the individual sources and uses of cash, and may be the only financial statement prepared for the period.

Audit reports on this financial statement should contain a separate paragraph that states the cash receipts and disbursements basis of accounting is being used and that it represents a comprehensive basis of accounting other than GAAP (see SAS No. 62, paragraph 5 (d) [AU 623.05(d)]). This extra paragraph is not required for full-disclosure compilation and review reports as long as the notes state the basis of accounting used and describe how that basis differs from GAAP (see Interpretation No. 12 of SSARS 1 (AR section 9100.42)). A compilation report on financial statements that omit substantially all disclosures must also describe the basis of accounting used if such disclosure is not provided on the face of the statements or in an attached note (see Interpretation No. 12 of SSARS 1 (AR section 9100.43)).

Illustrations of audit, review, and compilation reports on statements of cash receipts and disbursements follow:

A) Audit

We have audited the accompanying statements of cash receipts and disbursements of XYZ Company for the years ended December 31, 19X2 and 19X1. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the statements of cash receipts and disbursements are free of material misstatement. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the statements of cash receipts and disbursements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the statements of cash receipts and disbursements. We believe that our audits provide a reasonable basis for our opinion.

As described in Note X, the financial statements have been prepared on the cash receipts and disbursements basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the cash receipts and disbursements of XYZ Company for the years ended December 31, 19X2 and 19X1, on the basis of accounting described in Note X.

B) Review

I (We) have reviewed the accompanying statements of cash receipts and disbursements of XYZ Company for the years ended December 31, 19X2 and 19X1, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the cash receipts and disbursements basis of accounting described in Note X.

C) Compilation With Full Disclosure

I (We) have compiled the accompanying statements of cash receipts and disbursements of XYZ Company for the years ended December 31, 19X2 and 19X1, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

D) Compilation With Substantially All Disclosures Omitted

I (We) have compiled the accompanying statements of cash receipts and disbursements of XYZ Company for the years ended December 31, 19X2 and 19X1, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. The financial statements have been prepared on the cash receipts and disbursements basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (We) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the informative disclosures ordinarily included in financial statements prepared on the cash receipts and disbursements basis of accounting. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's cash receipts and disbursements. Accordingly, these financial statements are not designed for those who are not informed about such matters. [Amended February 1995.] (TPA 9510.07)

B.006 Compiled Financial Statements Not Adjusted

Inquiry — An accountant processes client input on a computer and produces monthly statements that do not include adjustments for changes in inventories, prepayments, and accruals, and do not include notes. Adjustments are recorded annually. Can the accountant state in his report that adjustments to make the statements not misleading have not been made?

Reply — No. The specific departures from GAAP must be disclosed. SSARS 1, *Compilation and Review of Financial Statements,* paragraphs 39 and 41, are clear that the accountant must consider whether a modified report is adequate to disclose the departures. SSARS 1, paragraph 40 describes the form of report when the accountant concludes that a modified report is appropriate. The departures should be disclosed in a separate paragraph, including the effects of the departures on the financial statements, if known to the accountant, or he should state that the effects have not been determined. (TPA 9600.01)

B.007 Inquiries for a Review Engagement

Inquiry — SSARS 1, *Compilation and Review of Financial Statements,* Appendix A, lists certain suggested inquiries for a review engagement. Is a "yes" or "no" response sought?

Reply — Appendix A states that the list is not intended to serve as a checklist, but to describe the general areas in which inquiries might be made. The inquiries in Appendix A are presented for illustrative purposes only. They do not necessarily apply to every engagement, nor are they meant to be all-inclusive. The accountant has to bear in mind that he must achieve limited assurance about the financial statements. His inquiry and analytical procedures should be designed to provide him with that assurance. A review should not be treated as a mechanical exercise to obtain "yes" or "no" answers to the illustrative inquiries. The accountant should exercise professional judgment based on all relevant circumstances in designing his inquiries and evaluating responses. While some of the inquiries can be answered "yes" or "no," others cannot because they are asking "what are the procedures. . ." (TPA 9600.02)

B.008 Financial Statements Marked As "Unaudited"

Inquiry — Should each page of compiled or reviewed financial statements of nonpublic companies be marked "unaudited"?

Reply — No. SSARS 1, *Compilation and Review of Financial Statements* (AR 100), does not require that each page of compiled or reviewed financial statements of a nonpublic entity be marked as "unaudited." Before SSARS 1 (AR 100) was issued, it was common practice to mark each page as "unaudited"; however, this practice was discontinued after SSARS 1 (AR 100) was issued because the phrase "unaudited" does not communicate to the reader the financial statement service performed.

SSARS 1 (AR 100) does require, however, that each page of the financial statements include a reference such as "See Accountant's Compilation Report" (AR 100.16) or "See Accountant's Review Report" (AR 100.34), as appropriate. [Amended February 1995.] (TPA 9600.04)

B.009 Supplementary Information

Inquiry — Are supporting schedules of balance sheet or income statement accounts considered supplementary information? If so, what are the reporting requirements in a review or compilation engagement?

Reply — SSARS 1, *Compilation and Review of Financial Statements,* paragraph 43, pertains to reporting on supplementary information that accompanies the basic financial statements in a review or compilation engagement. The basic financial statements are usually considered to be the balance sheet, statement of income, statement of retained earnings or changes in stockholders' equity, and statement of cash flows. Descriptions of accounting policies and notes to financial statements are also considered part of the basic financial statements and are usually identified as such, for example, by a legend on the balance sheet, etc., indicating that the notes are an integral part of the financial statements. If supporting schedules of balance sheet or income statement accounts are not identified as being part of the basic financial statements, they are considered supplementary information.

If the information does not accompany the basic financial statements, it is not supplementary information. Under SSARS 1, paragraph 4, it does not meet the definition of a financial statement, and therefore, the accountant does not have a reporting obligation. However, the accountant may want to issue a report to clarify his responsibility. This can be done by modifying the standard compilation report (SSARS 1, paragraph 17) to refer to the schedules. [Amended] (TPA 9600.08)

B.010 Application of SSARS 3 to Certain Companies Required to File With Regulatory Bodies

Inquiry — Some nonpublic entities, as defined in SSARS 2, *Reporting on Comparative Financial Statements,* paragraph 1, footnote 2, such as privately owned brokers or dealers in securities, may be required to include unaudited financial statements in a form prescribed by a regulatory body concerned with the sale or trading of securities, such as the National Association of Securities Dealers or the New York Stock Exchange. Does the first sentence of SSARS 3, *Compilation Reports on Financial Statements Included in Certain Prescribed Forms,* paragraph 2, preclude an accountant from using the alternative form of report illustrated in SSARS 3 in those circumstances?

Reply — No. SSARS 3, paragraph 2, excludes from the definition of a prescribed form those forms ". . . concerned with the sale or trading of securities." In that context, "securities" refers to those issued or to be issued by the entity submitting the prescribed form. Accordingly, an accountant is not precluded in the circumstances described in this question from using the alternative form of compilation report illustrated in SSARS 3 if the entity is not submitting the prescribed form in connection with the actual or contemplated sale or trading of its own securities. (TPA 9600.09)

B.011 Review of Financial Statements Included in a Prescribed Form

Inquiry — SSARS 3, *Compilation Reports on Financial Statements Included in Certain Prescribed Forms,* paragraph 3, states that "in the absence of a requirement or a request for a review report on the financial statements included in a prescribed form, the following form of standard compilation report may be used when the unaudited financial statements of a nonpublic entity are included in a prescribed form that calls for departure from generally accepted accounting principles . . ." Can an accountant perform a review of financial statements included in a prescribed form that are presented on a basis other than generally accepted accounting principles?

Reply — A review can be performed on the financial statements included in a prescribed form prepared under any comprehensive basis of accounting (as defined in SAS No. 62, *Special Reports,* paragraph 4), but SSARS 1, *Compilation and Review of Financial Statements,* reporting standards would apply, not those in SSARS 3. SSARS 3, paragraph 1, states in part:

The requirements of SSARS 1 and SSARS 2 are applicable when the unaudited financial statements of a nonpublic entity are included in a prescribed form. This statement amends SSARS 1 and SSARS 2 to provide for an alternative form of standard compilation report when the prescribed form or related instructions call for departure from generally accepted accounting principles by specifying a measurement principle not in conformity with generally accepted accounting principles or by failing to request the disclosures required by generally accepted accounting principles.

Accordingly, where the prescribed form calls for the departures referred to above, a review report expressing limited assurance under SSARS 1 would be appropriate provided that, as required by SSARS 1, paragraph 40, the review report discloses the departures from generally accepted accounting principles, including the departures called for by the prescribed form. (TPA 9600.10)

B.012 Computer Generated Financial Statements

Inquiry — A firm recently purchased a new computer which will enable it to have some of its clients access this computer via a phone terminal in their office. The client will input all information into the firm's computer including journal entries and will be able to prepare its own financial statements which will be received via the client's phone terminal. No one in the accounting firm directly inputs data into the computer or sees the financial statements. Is the accounting firm required to attach a compilation report for this type service?

Reply — No. If the client directly inputs data from its office into the computer and generates the financial statements in the client's office directly from the computer, the firm does not have a reporting responsibility. However, if the financial statements are generated by the CPA in the firm's office, there is a reporting responsibility as discussed in SSARS 1, *Compilation and Review of Financial Statements,* paragraph 7. [Amended] (TPA 9600.11)

B.013 Uncertainties/Going Concern Problems

Inquiry — SAS No. 59, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern,* provides guidance on that subject as it would affect the auditor's report under SAS No 58, *Reports on Audited Financial Statements*. What is the appropriate guidance on how to deal with uncertainties under the statements on standards for accounting and review services?

Reply — SSARS 1, *Compilation and Review of Financial Statements,* footnote 18 (AR 100.40, footnote 18), states that "normally, neither an uncertainty...including an uncertainty about an entity's ability to continue as a going concern, nor an inconsistency in the application of accounting principles would cause the accountant to modify the standard report provided the financial statements appropriately disclose such matters." Accordingly, disclosure of this uncertainty in a footnote to the financial statements would satisfy this requirement. SSARS 1, footnote 18 (AR 100.40, footnote 18), further states, "nothing in this statement, however, is intended to preclude the accountant from emphasizing in a separate paragraph of his report a matter regarding the financial statements."

The last two paragraphs of Interpretation No. 11 of SSARS 1, "Reporting on Uncertainties," indicates there is no requirement to disclose an uncertainty in the accountant's report, under certain conditions, when management has elected to omit substantially all disclosures required by generally accepted accounting principles. [Amended] (TPA 9600.14)

B.014 Consistency

Inquiry — A correction of an error in previously issued financial statements is treated as a prior period adjustment, in accordance with FASB Statement No. 16, *Prior Period Adjustments*. SAS No. 1, section 420, *Consistency of Application of Generally Accepted Accounting Principles,* paragraph 10, discusses a correction of an error in principle and states that a change from an accounting principle that is not generally accepted to one that is generally accepted, including correction of a mistake in the application of a principle, is a correction of an error. Although this type of change in accounting principle should be accounted for as the correction of an error, the change requires recognition in the auditor's report through the addition of an explanatory paragraph. How is this consistency issue treated in compilation and review engagements?

Reply — SSARS 1, *Compilation and Review of Financial Statements,* footnote 18 (AR 100.40, footnote 18), states that "normally, neither an uncertainty...including an uncertainty about an entity's ability to continue as a going concern, nor an inconsistency in the application of accounting principles would cause the accountant to modify the standard report provided the financial statements appropriately disclose such matters." Accordingly, disclosure of this inconsistency in a footnote to the financial statements would satisfy this requirement. SSARS 1, footnote 18 (AR 100.40, footnote 18), further states, "nothing in this statement, however, is intended to preclude an accountant from emphasizing in a separate paragraph of his or her report a matter regarding the financial statements." [Amended] (TPA 9600.15)

B.015 Reference to Accountant's Report in Notes to Financial Statements

Inquiry — SSARS 1, *Compilation and Review of Financial Statements,* paragraphs 16 and 34, requires that each page of the financial statements compiled or reviewed by the accountant include a reference such as "See Accountant's Compilation (or Review) Report."

Does this requirement extend to the related notes to the financial statements?

Reply — The application of this requirement varies in practice.

Some accountants believe that since the related notes to financial statements are an integral part of the basic financial statements, at least the first page of the notes should include a reference to the accountant's report.

Other accountants believe that if the basic financial statements, other than footnote disclosures, contain a statement indicating that the notes to financial statements are an integral part of the statements, it is not necessary to include a reference to the accountant's report on note pages. (TPA 9600.16)

B.016 Bank Engaged a CPA Firm to Compile a Financial Statement of Another Entity

Inquiry — A bank has engaged a CPA firm to compile a balance sheet for another entity. The bank has possession of the books and records of the entity. Can the firm issue a compilation report under such circumstances?

Reply — There is nothing in the Statements on Standards for Accounting and Review Services which precludes the CPA firm from issuing a compilation report under such circumstances. However, SSARS 1, *Compilation and Review of Financial Statements,* paragraph 11, states: "To compile financial statements, the accountant should possess a general understanding of the nature of the entity's business transactions, the form of its accounting records, the stated qualifications of its accounting personnel, the accounting basis on which the financial statements are to be presented, and the form and content of the financial statements." Due to the nature of the engagement, the CPA firm may not be able to attain a sufficient level of understanding of the entity's business as required by SSARS 1, paragraph 11, to issue a compilation report on the balance sheet, nor obtain sufficient relevant data to afford a reasonable basis for conclusions or recommendations in relation to any professional services performed, as required by Rule 201(D) of the AICPA Code of Professional Conduct (ET section 201.01D). (See SSARS 1, paragraph 3 (AR section 100.03)). [Amended] (TPA 9600.18)

B.017 Issuance of an Audit Report on Financial Statements Which Have Already Been Reviewed

Inquiry — If an accountant has issued a review report on a set of financial statements, may he later issue an audit report on the same set of financial statements?

Reply — Yes. Interpretation No. 3 of SSARS 1, *Compilation and Review of Financial Statements,* states that SSARS 1 does not prohibit the accountant from accepting an engagement to perform a higher level of service with respect to financial statements that have been previously compiled or reviewed. (TPA 9600.19)

B.018 Reissuance When Not Independent

Inquiry — An accountant performed a review in the prior year and a compilation in the current year. He was independent in the prior year but impaired his independence in the current year. May he reissue his review report on the prior year financial statements?

Reply — Yes. SSARS 2, *Reporting on Comparative Financial Statements,* paragraph 8, states in part, "A continuing accountant who performs a lower level of service with respect to the financial statements of the current period should either (a) include as a separate paragraph of his report a description of the responsibility assumed for the financial statements of the prior period . . . or (b) reissue his report on the financial statements of the prior period." The separate paragraph referred to in item (a), above, includes a statement that the accountant has not performed any procedures in connection with the prior period review engagement after the date of his review report as reflected in the example in SSARS 2, paragraph 12. (TPA 9600.20)

B.019 Income Taxes Omitted on Interim Financial Statements

Inquiry — The management of a Subchapter C corporate client have rationalized that there will be no income tax due by year end because they will pay year-end bonuses, pension contributions and/or purchase property and equipment to obtain accelerated depreciation deductions. Accordingly, its interim financial statements are prepared without a provision and estimated liability for income taxes.

(1) Is this in conformity with generally accepted accounting principles?

(2) How should the accountant's compilation report be presented?

Reply — (1) No. APB Opinion No. 28, *Interim Financial Reporting*, Paragraph 17, states:

> The amounts of certain costs and expenses are frequently subjected to year-end adjustments even though they can be reasonably approximated at interim dates. To the extent possible such adjustments should be estimated and the estimated costs and expenses assigned to interim periods so that the interim periods bear a reasonable portion of the anticipated annual amount. Examples of such items include inventory shrinkage, allowance for uncollectible accounts, allowance for quantity discounts, and discretionary year-end bonuses.

In addition the last sentence of footnote 7 of FASB Interpretation No. 18, *Accounting for Income Taxes in Interim Periods*, states:

> If an enterprise is unable to estimate a part of its "ordinary" income (or loss) or the related tax (or benefit) but is otherwise able to make a reliable estimate, the tax (or benefit) applicable to the item that cannot be estimated shall be reported in the interim period in which the item is reported.

Accordingly, where year-end bonuses ("ordinary" income) have not been estimated and included in the interim period, because the estimate is not reliable, then the tax benefit should be recorded in the period that the estimate (or actual) expense is reported in the financial statements.

(2) Following is an example of an accountant's compilation report that would cover this departure from generally accepted accounting principles:

> We have compiled the accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and cash flows for the year then ended in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.
>
> A compilation is limited to presenting in the form of financial statements information that is the representation of management. We have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them. However, we did become aware of certain departures from generally accepted accounting principles that are described in the following paragraph.

> It is management's intent to minimize or eliminate income taxes by paying year-end bonuses, pension contributions and/or purchasing property and equipment to obtain accelerated depreciation deductions. None of these potential transactions have been estimated, nor has a provision for income taxes been reported in the accompanying financial statements. Generally accepted accounting principles require that discretionary year-end bonuses and/or pension costs should be estimated and assigned to interim periods so that the interim periods bear a reasonable portion of the anticipated annual amount. If these amounts cannot be reliably estimated, then the tax consequence should be reported in the interim period in which the item is reported. (TPA 9600.21)

B.020 Reporting on Financial Statements Submitted by Management

Inquiry — A corporation's chief financial officer has been asked to prepare and submit his employer's financial statements to a bank. May the CFO use the standard compilation report?

Reply — No. The compilation report is inappropriate. A compilation report is used by an outside accountant to report upon financial statements that are the representation of another party, namely, the management of a nonpublic company. The compilation report describes the outside accountant's limited responsibility and inability to express an opinion or any other form of assurance based on the limited procedures performed. The CFO, on the other hand, is a part of management and is intimately involved in the preparation of the financial statements. A CFO has direct responsibility for the design and operation of the accounting system, the design and operation of most control procedures and much of the control environment.

There are no standards on how a company's CFO should report on the company's financial statements when those statements are transmitted to third parties. However, it seems appropriate for a CFO to issue a report stating management's responsibility for the financial statements. Such a report might be modeled after the management responsibility letter typically contained in annual reports and may be worded as follows:

> The accompanying balance sheet of Company X as of December 31, 19XX and the related statements of income, retained earnings, and cash flows for the year then ended have been prepared by management who is responsible for their integrity and objectivity. These statements have not been compiled, reviewed or audited by outside accountants.
>
> Company X maintains an internal control structure designed to provide reasonable assurance that assets are safeguarded and that transactions are properly executed, recorded and summarized to produce reliable records and reports.
>
> To the best of management's knowledge and belief, the statements and related information were prepared in conformity with generally accepted accounting principles, and are based on recorded transactions and management's best estimates and judgments.
>
> Signature as chief financial officer (TPA 9600.22)

B.021 Issuing a Compilation Report With Substantially All Disclosures Omitted After Issuing a Report on Financial Statements Containing Full Disclosure

Inquiry — A client wants to submit financial statements with substantially all disclosures omitted to one of its vendors. May the accountant issue a compilation report on those financial statements with substantially all disclosures omitted, if he or she previously issued an audit, review, or compilation report on financial statements with full disclosure for the same reporting period?

Reply — Generally, yes. This issue is not specifically addressed by the authoritative literature. However, SSARS 1, paragraph 19 (AR section 100.19), provides indirect guidance on this matter. It states that an accountant may compile financial statements that omit substantially all disclosures provided the omission of the disclosure is clearly indicated in the report and is not, to the accountant's knowledge, undertaken with the intention of misleading those who might reasonably be expected to use the financial statements.

If the accountant believes that the client's intent is to mislead users, the accountant should *not* comply with the request. However, if the accountant concludes that it is not the client's intent to mislead users, it would be appropriate to compile financial statements with substantially all disclosures omitted after having compiled, reviewed, or audited full-disclosure financial statements.

Some practitioners are reluctant to compile financial statements they have previously audited or reviewed because the accountant's compilation report will read:

> I have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

They conclude that the disclaimer in the report would be misleading to financial statement users in these circumstances because the accountant has, in fact, audited or reviewed the financial statements. They believe the aforementioned disclaimer precludes the accountant from compiling financial statements after auditing or reviewing them. The disclaimer in the compilation report, however, is intended to be engagement-specific and, therefore, refers only to the financial statements that accompany the accountant's report. Therefore, the disclaimer language does not present a reporting problem for the current engagement. (TPA 9600.24)

B.022 Break-Even Financial Statements

Inquiry — Company A requested compiled financial statements with an inventory reported so that the financial statements would reflect no profit or loss ("break-even financial statements"). How would this affect the accountant's compilation report?

Reply — "Break-even financial statements" are not in accordance with generally accepted accounting principles. Accordingly, the independent accountant would have to express a reservation in his compilation report because of the departure from generally accepted accounting principles as required by SSARS No. 1, *Compilation and Review of Financial Statements*, paragraph 40. (TPA 9900.06)

B.023 Compilation of Pro Forma Information

Inquiry — Statement on Standards for Attestation Engagements, *Reporting on Pro Forma Financial Information* (AT section 300) provides guidance on the examination and review of pro forma financial information. May an accountant issue a compilation report on pro forma information if the related historical financial statements are compiled?

Reply — Yes. Although the Statement on Standards for Attestation Engagements is silent with regard to compilation of pro forma information, it does not proscribe issuance of a compilation report on pro forma information. (TPA 9900.09)

B.024 Reports on Audited Financial Statements of a Nonpublic Entity Presented With Prior-Period Financial Statements Compiled or Reviewed by a Predecessor Accountant Who Has Ceased Operations

Inquiry — If the prior-period financial statements that have been compiled or reviewed by a predecessor accountant who has ceased operations are presented for comparative purposes with current-period audited financial statements, how is the successor auditor's report affected?

Reply — The answer depends on whether the prior-period financial statements have been restated.

a. If the prior-period financial statements are *unchanged,* the successor's report should make reference in a separate paragraph to the predecessor's report on the prior-period financial statements. This paragraph should include (1) a statement of the service performed in the prior period, (2) a statement that the predecessor has ceased operations, (3) the date of the report on the service performed, (4) a description of any modifications of that report, and (5) a statement that the service was less in scope than an audit and does not provide the basis for the expression of an opinion on the financial statements taken as a whole. Reference to the predecessor's report should not include the name of the predecessor. Examples of additional paragraphs for compiled and reviewed prior-period financial statements are presented below.

   Compiled Prior-Period Financial Statements

   The 19X1 financial statements were compiled by other accountants who have ceased operations, and their report thereon, dated February 1, 19X2, stated they did not audit or review those financial statements and, accordingly, express no opinion or other form of assurance on them.

   Reviewed Prior-Period Financial Statements

   The 19X1 financial statements were reviewed by other accountants who have ceased operations, and their report there-on, dated March 1, 19X2, stated they were not aware of any material modifications that should be made to those statements for them to be in conformity with generally accepted accounting principles. However, a review is substantially less in scope than an audit and does not provide a basis for the expression of an opinion on the financial statements taken as a whole.

b. If the prior-period financial statements *have been restated*, the restated prior-period financial statements should be compiled, reviewed, or audited and reported on accordingly. (TPA 9900.17)

B.025 Reports on Compiled or Reviewed Financial Statements Presented With Prior-Period Financial Statements Compiled, Reviewed or Audited by a Predecessor Accountant Who Has Ceased Operations

Inquiry — If prior-period financial statements that have been compiled, reviewed, or audited by a predecessor accountant who has ceased operations are presented for comparative purposes with current-period compiled or reviewed financial statements, how is the successor accountant's report affected?

Reply — The answer depends on whether the prior-period financial statements have been restated.

a. If the prior-period financial statements were *compiled or reviewed and are unchanged,* the successor should add a paragraph to his or her report on the current-period financial statements that includes (1) a statement that the financial statements of the prior period were compiled or reviewed by another accountant who has ceased operations, (2) the date of the predecessor's report, (3) a description of the standard form of disclaimer or limited assurance, as applicable, included in the report, and (4) a description or a quotation of any modifications of the standard report and of any paragraphs emphasizing a matter regarding the financial statements. Reference to the predecessor's report should not include the name of the predecessor. Examples of additional paragraphs for compiled and reviewed prior-period financial statements are presented below.

Compiled Prior-Period Financial Statements

The 19X1 financial statements of XYZ Company were compiled by other accountants who have ceased operations and whose report dated February 1, 19X2, stated that they did not express an opinion or any other form of assurance on those statements.

Reviewed Prior-Period Financial Statements

The 19X1 financial statements of XYZ Company were reviewed by other accountants who have ceased operations and whose report dated March 1, 19X2, stated that they were not aware of any material modifications that should be made to those statements in order for them to be in conformity with generally accepted accounting principles.

If the prior-period financial statements were *audited and are unchanged,* the successor should add a paragraph to his or her report on the current-period financial statements that indicates (1) that the financial statements of the prior period were audited by another accountant who has ceased operations, (2) the date of the predecessor's report, (3) the type of opinion issued by the predecessor, (4) if the opinion was other than unqualified, the substantive reasons therefor, and (5) that no auditing procedures were performed after the date of the predecessor's report. Reference to the predecessor's report should not include the name of the predecessor. An example of such a paragraph is presented below.

> The financial statements for the year ended December 31, 19X1, were audited by other accountants who have ceased operations, and they expressed an unqualified opinion on them in their report dated March 1, 19X2, but they have not performed any auditing procedures since that date.

b. If the prior-period financial statements *have been restated,* the restated prior-period financial statements should be compiled, reviewed, or audited and reported on accordingly. In addition, the successor should consider the guidance in paragraph B.026 below. (TPA 9900.18)

B.026 Successor Accountant's Responsibilities Under SSARSs When He or She Becomes Aware that Prior-Period Financial Statements Reported On by a Predecessor Accountant Who Has Ceased Operations May Require Revision

Inquiry — SSARS 4, *Communications Between Predecessor and Successor Accountants,* paragraph 10, provides guidance to a successor accountant who, during an engagement to compile or review current-period financial statements, becomes aware of information that leads him or her to believe that financial statements reported on by a predecessor accountant may require revision. SSARS 4, paragraph 10, states that the successor should request that his or her client communicate this information to the predecessor. How may the successor fulfill this responsibility when the predecessor has ceased operations?

Reply — When the successor becomes aware of information that leads him or her to believe that financial statements reported on by a predecessor who has ceased operations may require revision, the successor should request that the client advise the party responsible for winding up the affairs of the predecessor firm. If the client refuses to communicate with the predecessor or if the successor is not satisfied with the predecessor's course of action, the successor would be well advised to consult with his or her attorney. (TPA 9900.19)

B.027 Issuance of Review Report on Prospective Financial Statements

Inquiry — Is a review report appropriate for prospective financial statements?

Reply — No. The AICPA *Guide for Prospective Financial Statements* provides for only examination or compilation services or the application of agreed-upon procedures. (TPA 9900.20)

B.028 Use of Singular v. Plural Terminology for Accountants and Auditors

Inquiry — In reporting on audited, reviewed, or compiled financial statements, should accountants use singular or plural terminology when referring to themselves?

Reply — Use of plural or singular terminology is not addressed in the professional standards. Illustrative auditors' reports in Statements on Auditing Standards use plural terminology, while the accountants' reports in Statements on Standards for Accounting and Review Services use both singular and plural.

In practice, sole practitioners often use singular terms; firms that have one partner with professional staff use both singular and plural; and firms that have more than one partner most often use plural. However, the use of singular or plural references to the accountant or auditor is purely discretionary. For ease of report preparation, firms should be consistent in their use of singular or plural in all reports. (TPA 9900.25)

B.029 Compilation and Review—Comparative Financial Statements

Inquiry — A nonpublic entity's financial statements for the year ended December 31, 19X1 were compiled by a predecessor accountant. Management had elected to omit substantially all of the disclosures and the statement of cash flows required by generally accepted accounting principles (GAAP).

A successor auditor is engaged to audit the 19X2 financial statements, and the client has asked the auditor to include the 19X1 compiled financial statements for comparative purposes with the 19X2 financial statements.

Is the successor auditor permitted to do this?

Reply — No. SSARS 2, *Reporting on Comparative Financial Statements*, paragraph 5 (AR section 200.05), states that compiled financial statements that omit substantially all of the disclosures required by GAAP are not comparable to financial statements that include such disclosures.

The 19X1 financial statements would need to be revised to include the statement of cash flows and all disclosures required by GAAP. Either the predecessor or the successor accountant would then need to at least compile the full disclosure financial statements for 19X1. (TPA 9900.26)

Index

INDEX

References are to section numbers.

INTEGRATED
PRACTICE
SYSTEM

Titles Available in the AICPA Integrated Practice System Engagement Manuals Series

Comprehensive Engagement Manual	*(4 Volumes)*
Small Business Audit Manual	*(2 Volumes)*
Compilation and Review Manual	*(2 Volumes)*
Bank Audit Manual	*(3 Volumes)*
Credit Union Audit Manual	*(2 Volumes)*
Construction Contractors' Audit Manual	*(2 Volumes)*